UNFAIR TRADE PRACTICES

AND

SAFEGUARD ACTIONS

by ING-WEN TSAI

A Thesis Submitted for the Degree of PhD

The London School of Economics

The University of London

(1983)

To the London School of Economics and Political Science, my alma mater:

I began my graduate studies at the LSE in 1980, and during my time there, I completed my thesis, "Unfair Trade Practices and Safeguard Actions," passed the viva, and received my PhD degree. The LSE's rigorous academic environment trained me to become a better scholar and researcher, both tremendous assets throughout my career as a university professor, trade negotiator, and policymaker.

This thesis was completed in 1983. Clearly, the international economic landscape has changed a great deal over the past 36 years, yet non-tariff trade measures continue to pose a major challenge to global trade relations. Thus, I believe the historical background examined in my thesis is still worth reflecting on today.

I have recently authorized Taiwan's National Central Library to make my thesis available to the public to read and download. As the thesis I submitted upon graduation from the LSE is missing from the Library, I am also providing the LSE with a copy, and likewise authorize LSE to make it available to the public to read and download. I hope that this thesis may serve as a reference for future scholars of international trade and to commemorate my thesis advisor, Mr. Michael Elliott.

Ing-Wen Tsai

Tsai Ing-wen
October 3, 2019

Two copies to Taiwan

TO WHOM IT MAY CONCERN

This is to certify that Miss Ing-Wen Tsai, submitted a PhD thesis to the University of London in June 1983 and that an oral examination was held in mid-October 1983. The examiners have indicated their satisfaction both with the thesis and with Miss Tsai's performance in the oral examination, and have recommended to the University that the degree of PhD be awarded. It is expected that the official letter of award will be availabłe in February 1984.

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8 February, 1984

Dear Madam,

I am pleased to inform you that the Examiners for the degree of Doctor of Philosophy for which you are a candidate have reported that you have satisfied them in the examination:

Faculty: Laws

Field of Study: International Trade Law

Title of Thesis: Unfair trade practices and safeguard actions.

You will receive a diploma bearing the date of award of the degree after its formal conferment on the authority of the Senate or the Vice-Chancellor acting on its behalf.

Yours faithfully,

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To My Parents

ACKNOWLEDGEMENT

I am grateful to my superviser, Mr. Michael J. Elliott, for his guidance, patience and encouragement. I would also like to thank the following persons: Professor John J. Barcelo of Cornell University, USA, and Dr. B. Hindley of LSE, for their invaluable comments on the final part of this thesis; and Miss Tina Pei-Wen Sung whose inspiration, typing abilities and meticulous proof-reading helped greatly in the completion of this work.

ABSTRACT

As the world economy is now facing structural changes and recession unprecedented since the 1930s, trade protectionism has begun to re-emerge. Tariff trade barriers, after several rounds of GATT negotiation, are no longer a serious concern. Rather, it is the use of non-tariff trade barriers that threatens the world trading order. This thesis examines the legal problems involved in the use of the most commonly employed non-tariff trade barriers. The concentration is on dumping/ antidumping, subsidy/ antisubsidy, emergency safeguard actions against imports, voluntary export restriants (VERs), and the Multifiber Arrangements (MFA). Dumping and subsidy are commonly termed as unfair trade practices, although the element of unfairness in these practices is subject to much controversy. The emergency safeguard regimes under Article XIX of the General Agreement on Tariff and Trade (GATT), VERs, and the MFA present various modes of safeguard actions.

The thesis comprises three parts. Part One investigates the current state of world economy. Chapter I examines the impacts of structural changes and recession on the functions of three main international economic organizations, the GATT, the International Monetary Funds, and the United Nations Conference on Trade and Development. Chapter II looks into the classic free trade theory and the emergence of new sources of comparative advantages. Emphasis is on how the changing pattern of comparative advantage affect the world economy and trading relations. Current trade conflicts and their solutions are discussed in Chapter III with special emphasis on the various use of non-tariff trade barriers.

Part Two, the main part of this thesis, concentrates on the legal

analysis of those issues mentioned above. International law, mainly the GATT, as well as national implementing legislation and actual practices is investigated. Economic analysis is used to facilitate legal discussions.

Part Three, the concluding part of the thesis, has two chapters. Chapter I examines how politics in time of economic hardship affects the making and application of trade laws, and how far the current legal regimes regarding unfair trade practices and safeguard actions depart from the goal of global efficiency. Chapter II, in an attempt to search for the least distortive and politically viable way to improve the current legal order in international trade, discusses and comments on specific proposals made by Professor Barcelo of the Cornell University, Professor Lowenfeld of the New York University, and Dr. Hindley of the London School of Economics. Finally, the candidate puts forwards her own proposal.

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Introduction

Law and International Trade

The primary aim of human economic activities is to create wealth which in turn improves the quality of life. Behind such a simple aim, there are more complicated problems. How should these economic activities be managed in order to produce the maximum wealth? How should the wealth thus created be distributed? How and to what extent should the aim of maximizing wealth be reconciled with other values of human societies? Most importantly, how should law be designed to reflect the solutions to these problems?

These problems are less complicated and less difficult to solve in the domestic context. Residents within a national boundary may have a greater consensus on production and distribution patterns and on non-economic values. National governments may according to the consensus manage domestic activities by means of various legislations and regulations. Meanwhile, non-legal means can also be employed to remedy the deficiency of law. For instance, antitrust law may reflect the consensus that vigorous competition in the marketplace may maximize a nation's wealth through efficient allocation of resources. However, there may also be a preference that small businesses shall be protected no matter whether they can produce more efficiently than large companies. Thus, there are regulations aimed at restricting large companies to use their market powers improperly in competiting with small companies, such as the prohibition on using high profits reaped in one market to subsidize sales in another market, or using monopolistic buying power to buy materials at not-cost-justified low prices. Income tax legislation can be used as a means of income distribution. A government can even create social programmes to assist those who are less able to make a living under the economic system preferred by the majority of the nation.

In the international context, things are different. There is no such international government which is so powerful as national governments, in so far as management of economic activities is concerned. International consensus is not reflected in international legislation but in customs, treaties, and common interpretation of a specific issue. There are the sources of the so-called "international law".

What is the international consensus on the means of maximizing world income? The free trade theory, accepted by most of the trading nations, teaches that world income can be maximized only when there are free flows of goods, services, and capitals among nations. This is because without the existence of trade barriers both production and distribution of goods would only be governed by the law of comparative advantage. Thus, the production of goods would be carried out by more efficient producers who are able to produce more goods with less resources. Meanwhile, a country can concentrate its resources on the production where it is more powerful and hire the service where other countries are more powerful. Through efficient allocation of resources, there will be more goods for consumption at lower prices. The legal principle of open door, first seen in centuries ago in bilateral trading arrangements, is based on the rationale that free trade could maximize economic welfare. In the bilateral context, the application of the principle of open door means two parties to the arrangement wish to increase the economic welfare of each other through opening markets for goods from the other country. Residents of these two countries can enjoy more economic welfare than no trade at all. In the multilateral context, the application of the principle of open door means all the countries participating in the arrangement would open their markets to goods of whatever origins. Residents of all countries can enjoy even more economic welfare than what can be generated through bilateral application of the principle of open door.

Although absolute free trade can maximize world income, national governments are equally, if not more, concerned about distribution problem to which the theory of free trade fails to address. There is no international government that can serve as the distributor of world income. The problem of how world income should be distributed is even more difficult to tackle. The distribution problem is most acute to those countries which,as exporters or importers, had some degree of monopoly power before liberalization from a trade-barrier-ridden world. This is because these countries can by imposing import or export tariffs maximize their national welfare and trade liberalization would deprive them of such revenue. With the existence of pre-liberalization monopoly power, absolute free trade can be achieved only when there is an international government which is powerful enough to discipline those countries reluctant to give up their revenue from the use of optimum tariffs; or there is an international arrangement for the transfer of wealth to those countries to bribe or compensate for foregoing the revenue. Since both are not achievable because of practical and political difficulties, a method that can lead the world to a second-best position must be found. The principle of reciprocity when applied in the trade liberalization process, such as negotiation of tariff reduction, would lead countries to a more liberal trade position. This means trade can be liberalized to the extent that the economic advantage that a country gives and gains in trade liberalization would be equal. Thus, for those relatively weak monopoly powers, the application of the principle of reciprocity could lead them to a position closer to free trade than what the principle can achieve for countries with stronger monopoly power. This is because they have less to lose in trade liberalization.

Apart from the above mentioned case for reciprocity, there are other reasons for reciprocity in terms of distribution of world income. Under the classic free trade theory, a country could gain through trade liberalization from cheaper imports on the one hand, and better market access for its exports on the other hand. Trade liberalization would therefore have a positive effect on the country's economic welfare. The important assumption is that the country can shift its resources out of the production where foreign imports are cheaper, to the production where it has comparative advantages, and the adjustment is always possible and smooth. However, the assumption is only valid when the market is perfect and there are enough outlets that can sufficiently absolve the resources released from the inefficient production. The reality of the world is that there rarely exists a perfect market and, because of the limits in technological innovations and the development of more efficient production pattern, it is difficult to find enough outlets where those resources can be utilized. Moreover, some countries may be more capable of adjusting to changes in trade conditions in the liberalization process, and some are less capable. It is therefore possible that some countries will be the losers in trade liberalization and have a negative gain from it. Although there are other means to reverse a country's declining trading position by reducing distortions in the marketplace and accelerating adjustment process and the creation of new industries, countries which foresee the danger of being a loser in trade liberalization would prefer the incorporation of the principle of reciprocity in negotiations. The principle therefore becomes a guarantee that a country's share of world income would not be seriously deteriorated.

Such a principle is also important politically in the sense that a government can avoid any need for changes in governmental exchange rate or fiscal and monetary policy in response to a new trade imbalance. Meanwhile, a national government would need the principle of reciprocity to be included in trade liberalization, so that it is politically possible for it to enter international commitments to open its domestic markets. It can gain approval from its citizens by arguing that the suffering of domestic citizens resulted from import competition would be offset by the expansion in export sectors.

Other than the principle of reciprocity, the principle of equity also plays an important role in the distribution of world income. The principle of equity can frequently be seen in the developing countries' argument for an equitable share of world income. The rationale for a case of equity for developing countries is subtle and subject to various interpretations, but it is commonly accepted that there shall be special arrangements to give developing countries an equitable share of world income which the operation of the world economic system fails to realize. Various commodity agreements are aimed at maintaining commodity prices in order to prevent developing countries' terms of trade from deteriorating. The Generalized System of Preference is designed to give developing countries a bigger share of world trade mainly through preferential tariff treatment.

Another application of the principle of equity is the argument for retaliation against foreign unfair trade practices. Government subsidies, dumping, infringement of foreign patent or copyright and other practices are considered as unfair means of international competition. Dumping in most cases is not inconsistent with global efficiency, and subsidies in some cases are non-distortive. Moreover, subsidies are sometimes a necessary instrument for government policies. However, it is often argued that these practices are undesirable as they are in conflict with the notion of fairness in doing business and therefore prevent the importing country or other exporting countries from acquiring an equitable share of world income. That dumping is an unfair trade practice is largely derived from the argument that the dumper's ability to charge low prices in the importing market is made possible by its monopolistic position in his home market. This is because being a monopolist in his home market the dumper is able to charge high prices in that market, and use the high prices to subsidize low-price sales in the importing market. The root of unfairness is therefore lies in the existence of imperfect market structure of the exporting country,and exporters are supposely unjustified in taking advantage from market imperfection. The same rationale applies to subsidies. Government assistance to domestic sectors by fiscal means is called subsidy. Such government assistance is considered as an artificial and therefore unfair comparative advantage. The use of the notion of "fairness" in the case of dumping and subsidies as the basis for equity is subject to much controversy. It is never clear how the term "unfair" should be defined and there never exists a consensus in this regard.

In addition to the above mentioned principles regarding the maximization of and distribution of world income , there are principles that are primarily for the establishment of a framework for trade liberalization. They are the principle of non-discrimination and its further application--- the most-favored-nation clause. If absolute free trade is achievable, the principle of non-discrimination can certainly be rationalized on economic grounds, because free trade is by definition non-discriminatory. Since absolute free trade can not be achieved, there is only legal meaning for such a principle. This is further endorsed by the recent development which shows that the principle has no basis whatsoever in arguments for the benefits of a liberal international trade order. *1 The principle has an economic meaning only when the world is totally free from trade barriers and the principle is used to prevent the appearance of trade barriers resulted from discriminatory measures. Hence, world production and trade patterns determined by the law of comparative advantages will not be disturbed by artificial advantages or disadvantages created by discriminatory measures. However, the world in reality is far from free of trade barriers. It is probable and very likely that the scale and the speed of liberalization from a trade-barrier-ridden, as opposed to a barrier-free, world would be greater without the application of the principle of non-discrimination. Moreover, if trade liberalization can lead to a barrier-free world, the principle will certainly have an economic meaning. However, as mentioned previously, because of the existence of pre-liberalization monopoly power, the difference in individual countries' abilities in adjusting to changes in the liberalization process, and the lack of a powerful international government to serve as the distributor of world income, absolute free trade is in reality not achiveable.

The principle of non-discrimination is largely derived from the notion of soverieignty equality which itself is a legal fiction. Such a legal fiction is of particular importance in establishing a framework for managing world economic relation, as it simplifies and therefore makes possible the weighing of each actor, i.e. each participating country in trade liberalization.

The MFN clause requires that a treatment granted to a specific trading partner in exchange for benefits received from it be applied to all other trading partners participating in a multilateral treaty. The clause also appears in a bilateral treaty, according to which each party to the treaty is obliged to grant the other party no less favorable treatment than whatever it grants to any third country. The MFN clause is particularly helpful in accelerating the process of tariff reduction. The clause when incorporated into a multilateral treaty is the best safeguard for those weak participating parties against discrimination based on political or economic strength of each party.

There may also be a principle of preference in a multilateral treaty allowing exceptions to its MFN clause. The incorporation of such a principle may be for the reason that two or more participating parties to the treaty wish to have a closer economic ties between them and grant preferential treatment to each other. The ultimate aim of such arrangement may be more integration, both economically and politically, between them.

The above mentioned principles are all incorporated into the post-war multilateral trading system operating under the General Agreement on Tariffs and Trade (GATT). The GATT was originally a multilateral treaty aimed at reduction of trade barriers, mainly the tariff wall built up in the inter-war economic slump. When the post-war trading community failed to establish an international organization for the management of world trade, which covers a much wider spectrum of issues than reduction of trade barriers, the GATT gradually expanded from a treaty with narrower concern to an organization in charge of nearly every aspect of world trade.

How are these principles applied under the GATT system? As the primary aim of the GATT is the liberalization of world trade, the principle of open door is the basis for those fundamental GATT rules refraining contracting parties from the use of various trade barriers, such as import/export quotas, and those invisible trade barriers in the import/export administration, e.g. imposing unreasonable quality control on import goods. The principle also provides the underlying rationale for negotiation on reduction of tariff barriers.

As to the principle of non-discrimination, there are GATT rules prohibiting discriminatory customs practices including import charges and duties, and requiring national treatment on taxation and regulations be accorded to foreign imports. All import and export restrictions when exceptionally permitted by the GATT rules shall be applied on a non-discriminatory basis, except those which are discriminatory by nature, such as antidumping and countervailing duties, and import control for the reason of national security or public health and safety. An area of special interest is the non-discriminatory application of safeguard measures under Article XIX of the GATT. The combined use of the principles of non-discrimination and reciprocity is the best protection of developing countries' interest when facing safeguard action by an importing country. We shall examine this issue further after the discussion of the principle of reciprocity.

The principle of reciprocity is mainly used as the guiding principle of negotiations on tariff reduction and regulations regarding the use of non-tariff trade barriers. The application of the principle in such a context is like this: the concessions a contracting party gives to other parties would be reciprocated by the concessions it gains from the latter. In the case of tariff reduction, there is no objective criteria in determining whether reciprocity has been achieved. Rather, it is the subjective satisfaction of each party participating in the negotiation to serve as such. In the case of non-tariff negotiation, a party's commitment to comply with the multilaterally agreed rules regarding the use of non-tariff trade barriers would be reciprocated by the same commitment from other parties. Reciprocity is also the fundamental concept in GATT litigations, because only those contracting parties whose benefits under the GATT are nullified or impaired by other parties' action or inaction would have a cause of action against the latter. The basic form of benefits under the GATT is the balance of economic advantages that contracting parties have achieved in previous rounds of negotiation. Balance of economic advantages is of course an application of the principle of reciprocity.

As mentioned previously, the principle of reciprocity makes trade liberalization possible, because it provides a guarantee that a country's terms of trade would not be seriously deteriorated as a result of trade liberalization. However, its application also imposes limitation on the extent to which trade can be liberalized. This is especially true in the case of tariff reduction. Such limitations can be eased to a large extent by MFN application of the negotiation result. This means the rate of tariff reduction that two contracting parties has reached regarding a specific product shall also be applied to all other countries participating in the negotiation. Although reciprocity has been reached between the first two parties, it is not necessarily so between either of the two parties and other countries. Under such circumstances, reciprocity between the first two parties and other parties is to be measured in approximation and presumed to have been accomplished in the sense that the first two parties can also enjory tariff reduction rates reached between other parties.

The combined application of the principles of reciprocity and non-discrimination in taking market safeguard action under Article XIX goes like this: when an importing country takes safeguard action to protect its domestic industry from being seriously disrupted, it shall apply safegurd measures non-discriminatorily among all imports and offer compensation to, or be subject to retaliation from, exporting countries. Compensation or retaliation under such circumstances is an application of the principle of reciprocity. This is because by taking safeguard action through increases in import tariffs or imposition of import quota, the importing country impairs the benefits that the exporting countries have paid for by granting the importing country equivalent (theoretically) concessions to exports from the importing country. Since the balance of advantage is damaged by a safeguard action, the importing country should offer compensation or be subject to retaliation to attain an equilibrium position though at a different level. Since safeguard action is governed by the principle of non-discrimination, compensation or retaliation is to be applied to all the exporting countries, and the cost of taking a safeguard action would be a heavy burden to the importing country. Consequently, the importing country may be deterred from abusing safeguard actions. This is particularly important to developing countries whose exports of labour-intensive products are often the target of safeguard actions by developed countries, and whose status as newcomers in the marketplace often makes them being identified as the source of disruption in the importing markets.

As regards to the application of the principle of equity, the GATT recognizes the need for granting special treatment to developing countries. Developing countries are allowed to deviate temporarily from the general restrictions of the GATT. Moreover, in order to improve their market accesss and therefore increase their revenue from exports, the GATT encourages developed countries to grant preferential tariff treatment to exports from developing countries. To facilitate such preferential arrangements, the GATT allows developed countries to depart from the principle of non-discrimination in so far as exports from developing countries are concerned. Meanwhile, the principle of reciprocity is not applied in trade negotiation between developed and developing countries. Tariff concessions granted by developed countries to developing countries are not necessarily to be reciprocated by concessions from the latter. Lieniencies are also granted to developing countries in the regulation of non-tariff trade barriers, while developed countries are subject to the general rules. Use of non-tariff trade barriers by developing countries would in many instances not be met with counteractions or constitute a cause of action for other countries.

Dumping and subsidy practices are considered as "unfair" trade practices and therefore contrary to the principle of equity. When they cause material injury or threaten material injury to the domestic industry of an importing country, they would be met with unilateral counteraction by the importing country in the form of antidumping or countervailing duties. Improper antidumping or countervailing duty administration, however, is considered as a non-tariff trade barrier.

Preferential arrangement among a group of countries are allowed in the case of customs unions and free trade areas. Pre-existing economic ties, such as British Commonwealth group and colonial ties between European and African countries,are allowed to continue as the basis for preferential arrangements.

The substance and relative importance of the principles discussed above would vary with changes in the world economy. What are the impacts of structural changes in the world economy since the late 1960s and the current recession on the application of these principles? First, they have imposed heavy pressure on the pursuit of trade liberalization,i.e. they have prevented further, if not tightened, application of the principle of open door. The movement of trade liberalization has been in a static condition, and as the recession goes on and deepens, there gradually emerged a reverse trend toward protectionism. Countries, who are cyclical or secular losers in international competition, are reluctant to keep their market open. The grievance from mass unemployment is so great that national governments in particular, and citizens of these nations in general, tend to neglect the benefit that they can gain from free trade. This is so even in economic terms a country's benefit from and cost of trade are still in balance. Because the cost falls on a segment of the population and the benefit spreads across all segments, the cost may appear, as the country perceives, greater than the benefit. Moreover, what is politically important is the number of citizens that are adversely affected by imports rather than the size of the cost. In developed countries, the cost of trade mostly falls on those labour-intensive manufacturing sectors and the benefit is however from exports of high technology goods where much less labour is needed. This, together with the fact that the increase in consumer welfare is so wide-spread that the gain from trade to each consumer may appear much less than the cost to individuals in the import-competing sectors, may make a government prefer less unemployment at the expense of free trade, namely,a poorer nation with less of its citizens unemployed.

There is also a tendency to change the meaning of reciprocity. As mentioned previously, reciprocity in trade negotiation when applied together with the MFN clause is to be measured in approximation. Under such circumstances, reciprocity is only theoretically accomplished.However, in practical sense, some countries may gain more and some less under such a negotiation pattern. This is because reciprocity is only in practical sense achieved between two countries, and either of them may not be able to gain reciprocity with a third country. Even after the negotiation pattern had been changed from country-by-country to across-the-board, the situation remains. According to the across-the-board pattern, all participating countries agree on a tariff reduction formula to be applied to all goods from whatever source. Reciprocity is an abstract concept under such circumstances, and in practical sense a country's gain and cost of trade with another country may be far from equivalent. Such application of the principle of reciprocity is viewed by secular and cyclical loser countries as not an equitable way of distributing benefit and cost of trade. They are instead tempted by the joint use of the notion of over-all reciprocity and discriminatory treatment. This means a country would give discriminatory treatment to imports from different countries to ensure that the over-all advantages each of these countries gains from the first country are equivalent to what it would gain from each of them. Such application of the principle of reciprocity would greatly undermine the principle of MFN treatment and be disastrous to the efforts toward free trade. Indeed, it may frustrate the whole post-war multilateral trading system and replace it with a world of bilateralism.

The joint use of the principles of reciprocity and non-discrimination in the case of market safeguard is under heavy pressure from protectionist forces. As the need for safeguard action is increasing, countries find such a joint use to be a barrier for them to practice protectionism. In the recent Tokyo Round negotiations, some developed countries, notablly the EEC, were pressing hard for the removal of the non-discrimination restriction and the obligation of compensation. It is very likely that in the Safeguard Code now pending negotiation there will be exceptions to the principle of non-discrimination and limitations on the right of compensation or retaliation.

The principle of equity is in danger of being abused in the case of retaliation against dumping and subsidy practices. As modern governments are more and more involved in domestic economic activities, government intervention has become common. This is especially true in time of structural changes and recession. Government assistance is necessary to accelerate domestic adjustment process to meet structural changes or to slow down the pace of structural changes in order to minimize the domestic dislocation cost. Subsidies may also be used as an instrument to achieve a social goal preferred by the nation as a whole. Dumping is a means for exporters to survive from economic downturns by using high domestic prices to subsidize foreign sales in order to maximize profits or minimize loss, and in most cases is consistent with global efficiency. Both dumping and subsidy practices are argued by some, especially cyclical and secular losers, as unfair trade practices, and therefore used as the justification for them to practice protectionism. With greatly expanded definition of subsidy and dumping, some importing countries are using antidumping and countervailing duties to practice protectionism to an extent well beyond the original meaning of "unfairness". For instance, antidumping duties are levied on imports sold at a price lower than cost of production and other costs plus a "reasonable" profits, no matter whether there exist price differentials between the home market and the importing market.

Through the changes in the substance of the legal principles discussed above and in their relative importance, one can see a world of increasing protectionism. The ideal of an efficient world where world income can be maximized seems even more remote. Moreover, the GATT, the organization built on these principles for the management of world trade is now facing serious challenge.

Purpose of This Thesis

This thesis is not intended to be a comprehensive study of the changing face of the international legal structure. Rather, it is concentrated on the study of subsidy/antisubsidy, dumping/antidumping, and emergency market safeguard, and specific application of the general legal principles in these regards. As these laws are most frequently used as protectionist instruments, changes in the application of the general principles are most drastic and their effects are most significant in so far as world trading as well as legal order is concerned.

This thesis first observes the function of, and the impacts of the structural changes and current recession on, three international organizations associated with the management of world trade. The classic free trade theory and its modern content are examined with a view to seeking possible justifications for imposing limits on free trade. The intention is to demonstrate the economic rationale behind government action in regards to subsidy, antidumping, antisubsidy, and emergency safeguard within the general framework of free trade theory. Current trade conflicts are also investigated to demonstrate how the post-war legal order has been damaged and the role that subsidy/antisubsidy, dumping/antidumping and market safeguards played in these conflicts.

These background studies are followed by comprehensive investigation on economic as well as legal aspects of these three regimes. As international trade law is a reflection of the international consensus on the running of the world economic system, the pattern of income distribution, and non-economic values, this thesis in analyzing these regiemes uses the notion of efficiency as the main technique supplemented by distribution and non-economic considerations.

The legal as well as economic analysis of Part Two will be followed by an assessment of each of the trade laws under consideration in Part Three, in an attempt to find out the political elements in their making and application and the relative possible trade effects of these laws.

The results of the above investigation will be used in Chapter II of Part Three where efforts are made to seek a politically viable means to remedy current legal disorder. A well designed safeguard system may give an importing country reasonable room for the assertion of protectionism when it perceives that the cost of trade exceeds the benefit either in economic or in social terms. It can therefore be prevented from deserting the commitment of trade liberalization totally. This thesis sees the feasibility of a sectoral safeguard approach which would allow exceptions to the principle of non-discrimination and the obligation of compensation for those sectors most affected by structural changes and recession. Such a sectoral framework should be carefully designed so that it will not have adverse effects on the whole legal system. Such a device may lightened the pressure for more use of anti-dumping and countervailing duties, and make it possible to tighten the general safeguard system. In addition to this sectoral safeguard approach, this thesis also proposed plans with regard to antidumping and countervailing duty and general safeguard laws. These plans are intended to prevent current legal orders in these regards from deteriorating and to seek positive improvement through multilateral efforts.

As mentioned previously, the social cost of trade in a time of structural changes and recession is so great that national governments and their citizens tend to neglect the benefit of trade. The greatly inflated social cost is the source of political pressure for protectionism in those cyclical and secular loser countries. The scale of social is not to be determined by objective judgement and very much depends on the subjective perception of citizens of trading countries. Although protectionist pressures cannot be justified on rational (or economic) grounds, their existence must be recognized as a reality in seeking legal reforms. This candidate wishes to stress that the proposals of her thesis are directed at improvement in legal orders in time of economic hardship, and therefore may appear conciliatory to some extent to the protectionist trend. Though conciliatory, these proposals are the maximum reforms that can be attained in view of strong pressure for protection. This candidate also recognizes the possibility of more radical reform when the current recession is over and structural changes can proceed with less dislocation cost.

Note 1: H.G. Johnson, ' Trade Negotiations and the New International Monetary System ', pp.18

PART ONE

A WORLD IN TRANSITION

PART ONE: General Background --- A World in Transition

Chapter I: Institutionalization of International Economic Cooperation

The most important feature of the post war world economy is the institutionalization of international cooperation. This is due to the consensus that the chaos arising from the financial crisis and the ensuing protectionism in the inter-war economic slump should not be allowed to reappear. Under the lead of the U.S., efforts have been made to achieve an open, liberal, and multilateral international economic order. Two important principles were followed, namely, multilateralism and functional seperativism. The adoption of the multilateralism is to prevent the disorder usually associated with nationalism or bilateralism which dominated the economic relations in the 1930s. Multilateralism can provide a mechanism to balance the interests of individual countries and to ensure that the balance would not be damaged by unilateral measures or bilateral arrangements. Functional seperativism is meant to establish seperate international institutions to perform different functions. For instance, the concern of the General Agreement on Tariffs and Trade (GATT) is the management of world trade, and the International Monetary Funds (IMF) is in charge of international monetary arrangements.

In the following sections, three most important international economic institutions will be discussed. They are: the GATT, the IMF and the United Nations Conference on Trade and Development (UNCTAD). The discussions will also cover how the structural changes in the world economy and the current recession affect their functions.

(A) The General Agreement on Tariffs and Trade *1

The GATT is the presiding element in the management of world trade. Interestingly, the GATT, in the minds of those national leaders who initiated the development towards an organized trading system, was not intended to play the central role. Instead, the International Trade Organization (ITO) was to serve as such. The efforts to set up the ITO was frustrated by the U.S. Congress of the late 1940s which was less liberal in trade matters and less internationally oriented. The responsibility of regulating tariffs, quotas, taxes, and international commodity agreements was therefore assumed by the CATT, an agreement criginally drafted as a subsidiary of the ITO Charter to embody the results of tariff negotiations. How did the GATT adapt itself from a tariff agreement to a presiding controller of world trade? It achieved this through the greatly expanded notion of tariff.

The first mission of the GATT was to dissolve the high tariff wall built up in the inter-war economic slump. Each contracting party under the General Agreement is obliged to make tariff concessions to others in multilateral negotiations. To ensure that the benefits resulting from tariff reduction would not be nullified or impaired by the use of non-tariff measures having the same or similar effects as those of tariffs, the GATT went a step further to cover non-tariff trade barriers. Several articles of the General Agreement were designed to regulate such issues as antidumping administration,*2 quotas,*3 internal taxes, charges and regulations affecting trade flows,*4 customs valuation,*5 fees and formalities connected with importation and exportation,*6 mark of origin,*7 publication and administration of trade regulations,*8 subsidies,*9 and countervailing duties.*10 By the late 1960s, when tariffs were no longer a significant barrier to trade as a result of several rounds of negotiation, non-tariff barriers emerged as an alternative measure of protection. From then on, the GATT shifted its emphasis to the control of non-tariff trade barriers, a difficult task that was avoided before. The International Antidumping Code of 1967, negotiated during the Kennedy Round, was the first attempt. The tendency of using non-tariff trade barriers as protective devices was increasing in the following years. The task of the Tokyo Round negotiations (also known as Multilateral Trade Negotiations, MTN) is therefore to establish a comprehensive scheme for disciplining the use of non-tariff trade barriers, and several codes of conduct were produced. The Codes are: the Subsidy/Countervailing Duty Code,*12 the Customs Valuation Agreement,*13 the Agreement on Import Licensing Procedures,*14 the Agreement on Standards (Technical Barriers to Trade),*15 and the Agreement on Government Procurement.*16

The GATT further expanded to involve itself in such issues as employment problems, economic development of developing countries and international cartels. At first sight, these issues do not seem to be strongly related to the GATT's concern on tariff reduction. The Multifiber Arrangement*17 is the typical example of GATT's concern about the employment problems in the developed countries. The conclusion of this arrangement is due to the fear that facing mass unemployment, importing countries may resort to tariff or non-tariff measures to protect their domestic textile industries. A special arrangement can have the effect of slowing down market penetration of foreign imports in the absence of tariff protection and allowing time for adjustment. In the case of economic development, the GATT is concerned about special tariff reductions and non-reciprocal treatments regarding non-tariff matters to developing countries.*18

This is intended to increase their revenues from exports so that they are able to finance development projects. Involvement in international cartels, such as the International Dairy Agreement*19 and the Agreement Regarding Bovine Meat*20 concluded in the Tokyo Round, is due to the fact that many non-tariif measures such as subsidies, dumping and quotas are used in agricultural product trade.

The most important principles that underline the operation of GATT law are that of most-favored-nation treatment and of national treatment. The MFN principle is provided in Article I of the General Agreement. Each contracting parties is required to extend the favorable treatment it grants to another party to all parties of the General Agreement. The MFN has the advantage of spreading tariff reduction faster than it would be through conditional MFN or no MFN at all. Exceptions are allowed in the following areas: (1) waiver for Generalized System of Preference(GSP) for developing countries,*23 (2) national security,*24 (3) balance of payments difficulty,*25 (4) customs unions and free trade areas, *26 and (5) general health and welfare.*27 In addition, preferential arrangements, due to historical ties such as British Commonwealth group and colonial relationships between European and African countries, are allowed to continue.*28

The national treatment clause*29 requires a country to treat imports, once they have crossed the border and cleared customs, the same as domestic goods. The application of the clause is more frequent in regulating non-tariff trade barriers. Controversies arising from border tax adjustments and safety regulations are often related to the national treatment clause.

The expansion of the GATT demonstrates the transformation from an agreement to an international institution performing as the manager of world trade. Since its original form was an agreement among trading nations, the GATT lacks an organizational charter which is essential to the formation of international institutions, particularly those of supra-national nature. Under a supra-national institution, liberalization of world trade can be much more effectively achieved. Moreover, as the GATT is a multilateral contract rather than an organizational charter, the decision of its adjudicating bodies is only equivalent to an arbitration or conciliation award without being backed by national courts.*30 The only formal mechanism avialable to enforce the award is withdrawal of concessions. Are all these enough to support the expansion of the GATT in an era of rising protectionism? The issue will be examined in Chapter I of Part Two.

(B) International Monetary Fund *31

The IMF was established in the Bretton Woods Conference as the central institution in charge of world monetary arrangements. The IMF Agreement is a combination of an organizational charter and rules of conduct for member states. There are three mechanisms for the IMF to maintain the world financial order. First, to maintain monetary stability and to prevent competitive devaluation, member states are required to cooperate with the Fund and other members to ensure an orderly exchange arrangement and to promote a stable system of exchange rates.*32 Thus, they should establish par values for their currencies, and to maintain them by necessary government intervention.*33 Depreciation or revaluation is not allowed except for the purpose of correcting fundamental disequilibrium.*34 As the value of a currency was fixed in terms of U.S. dollar which in turn was set in terms of gold prices, the delay in effecting an exchange rate realignment in response to the inflation in the mid-1960s resulted in U.S. balance of payments deficits and a very sharp increase in international reserves of the Western Europe and Japan. This disturbance is turn was the main contributor to the inflation of the early 1970s.*35 In the Smithsonian Conference of 1972, the dollar was allowed to devalue and the margin of the permitted fluctuaction was widened.*36 The subsequent sharp increase in inflation rates resulted from the oil crisis and substantial differences in acceptable inflation rates among individual countries initiated the move towards a flexible exchange rate system.*37 In a summit conference in 1975 of the prime ministers and presidents of industrialized countries, the floating exchange rate system was accepted under the condition that there should be consultation among financial ministers and central banks so as to maintain order.*38 The Jamica Accord of 1976 further legitimized the existing mix of floating and pegged exchanged rates (or managed floating rates).*39

Second, in setting up a multilateral system of payment, the Fund requires member states to refrain from imposing restrictions on current account payments and exercising discriminatory currency practices, to buy balance of its currency held by another member upon request, and to furnish the Fund with information.*40 Third, various funds were established to finance countries in temporary balance of payments difficulties. In addition, as annual increases in international credit appeared insufficient to meet the increasing volume of world trade, a new form of liquidity, special drawing right (SDR) was created with the intention that SDRs would in the future replace national currencies and gold as the means of reserves. Thus, those obstacles to the growth of world reserves as a result of trade deficits of the countries whose currencies are used as components of reserves or of changes in the policies of gold-producing countries can be eliminated.*41

Since its establishment, the Fund performed as an effective stablilizing force in international financial arrangements untill the late 1960s. The Great Inflation of the early 1970s have enormously affected the stability of monetary arrangements. Monetary instability in turn has threatened the open and non-discriminatory trading system and aroused the re-emergence of protectionism. The arrangements of the Smithsonian Argreement and the move to floating exchange rates did ease the early financial crisis to some extent. However, later disturbance resulting from drastic increases in oil prices further intensified deficits and inflation. Countries following contractive monetary policies, such as West Germany and Japan, were able to maintain trade surpluses large enough to cover their oil bills. Moreover, the refusal to appreciate their currencies to reflect the real values shifted the burden of deficits to countries who did not adopt the same policies either because they favored import generated deficits so as to limit the increase in domestic price levels; or because they felt that contractive policies would lead to higher unemployment and threaten political stability.*42 Inconsistency in national monetary policies necessitated international cooperation to distribute the burden of deficits and to establish criteria for government intervention in the exchange market. Harmonization of national policies could temper fluctuations in exchange rates. In addition, orderly arrangements were particularly important to developing countries having large foreign trade sectors. The Jamaica Accord, however, did not prescribe the form of exchange market behaviour. It seemed that the Fund was virtually excluded from the summit meetings of the leaders of industrial countries where monetary policies were consulted. At present, more far-reaching reform seems unlikely. This is due to the fact the substantial uncertainties about the size of OPEC trade and surplus, differences in acceptable rates of inflation, and divergence in political relationships deter major industrial countries from entering into long-term commitments.*43

(C) <u>The United Nations Conference on Trade and Development</u>

The wide gaps between the average incomes of developed and developing countries and between their rates of economic growth give rise to the so-called development problem, also known as the North-South problem.*44 The efforts to solve the development problem were mostly made under the U.N. system. Developing countries, through the non-alliance movement, group themselves as an united bloc (also known as Group of 77) and use the U.N. facilities to assert their demands. The endeavours were first materialized in the first U.N. Conference on Trade and Development (UNCTAD I) held in Geneva in 1964. The final act adopted in that conference , although denied binding force by developed countries, formed the basis for demands of developing countries in subsequent international conferences. After the Geneva Conference, the UNCTAD began to be institutionalized and gradually became the "trade union" of developing countries. It also gathers many experts with various disciplines to conduct investigation on every issue of special interest to the economic development of developing countries. With regard to the improvement of market access and the stability of monetary arrangements as well as the financing of economic development, the UNCTAD established necessary links with the GATT and the IMF and its subsidiaries, making proposals to the two institutions to reflect the needs of developing countries. The most important influence of the UNCTAD on the GATT system is a new chapter on trade and development added to the General Agreement in 1965, which calls for the reduction of tariffs and other trade barriers in regard to exports from developing countries. This made possible the incorporation of the Generalized System of Preference into the GATT system structured on the MFN principle. The GSP, primarily intended to be applied to tariff reductions, was further extended to the non-tariff measures in a more unified pattern when the GATT shifted its emphasis to the control on non-tariff trade barriers. The UNCTAD compiles data regarding trade barriers, especially those of non-tariff nature, and provides assistance to the GATT with regrd to development issues.

While the UNCTAD was able to make progress in areas where the interests of developing and developed countries are less conflicting, such as the Code of Conduct for Liner Conferences, many of its proposals are lacking actions to implement. Moreover, although some of the proposal could gain legal recognition through the U.N. machinery in the form of resolution or declaration because of the majority of developing countries, actual implementation was found difficult to attain largely due to the incooperative attitudes of developed countries. Moreover, unlike the GATT or the IMF, the UNCTAD is rather an affiliate of the U.N. than an independent institution having a more advanced organizational structure and an enforcing mechanism that can impose sanction in one way or another to ensure compliance. This, together with other organizational weakness inherent in large conferences, further deters the UNCTAD from being an effective machinery in bridging the gap between developed and developing countries.

Developed countries would prefer the development issue to be dealt with in the GATT or the IMF where the decision-making would not be dominated by the sheer number of the participating developing countries. Some developed countries also take the position that the development problem should be solved through improved market access for developing countries' exports rather than out right aid-giving. However, this position is contradicted by the facts that many developed countries are becoming more and more protectionist, and that the present unstable international monetary arrangements are extremely pernicious to the trade position of developing countries. Moreover, the prevailing high interest rates and the pressure from some developed countries on the IMF to tighten its credit policies not only increase the debt burden, but restrict the access, to both official and private capital markets, of developing countries.

CONCLUSION

The liberalism in trade and monetary policies that prevailed after the war has produced a prosperity never envisaged in human history. This is largely made possible by stable monetary arrangement and low energy cost. From the late 1960s, the world economy went into an era of chaos with only few short periods of upturn. The U.S. balance-of-payments deficit and the world-wide inflation of the late 1960s,resulting from America's being the world central banker for several decades and its large foreign spendings, inflicted the first blow to monetary stability. Although this was eased to some extent by the monetary arrangement of the 1970s, the sudden and huge increase in oil prices gave rise to another even bigger inflation. Non-oil producing countries began to feel the deficit pressure and many of them began to pursue contractive policies. A world of fast expanding is no longer in existence. This is further intensified by the re-emergence of protectionism. The sign of serious recession is clearly in sight.

In the meantime, the world economy also went into a structural change largely because of technology innovation and high labour cost in developed countries. The labour-saving feature of modern technology and the increasing competitiveness of developing countries in the production of labour-intensive products resulted in serious unemployment problems in developed countries. The pressure for protection against imports from developing countries has therefore been increasing.

The three major international economic organizations are inevitably affected by these events. While the GATT is expanding to cope with the increasing use of trade barriers, there is a fundamental problem as to the adequacy of its enforcement mechanism. The IMF is unable to impose institutional discipline on international monetary arrangements to provide monetary stability for the running of economies. The economic hardship of developed countries has hampered the UNCTAD's effort to bridge the gap between economic prosperity of developed and developing countries.

Footnotes (Part One , Chapter I)

1. The standard source of the history of the GATT is the 'Multilateral Commercial Diplomacy' by G. Curzon. For GATT-related current trade issues, the London based Trade Policy Research Center has published a large amount of studies by comtemporary economists. For GATT-related legal problems, see K.W. Dam, 'The GATT Law and International Organization'; L. Lazar, 'Transnational Economic and Monetary Law, Transactions and Contracts'; J.H. Jackson, 'Legal Problems of International Economic Relations, cases, materials and text' Chapter 7-18, and 'World Trade and the Law of GATT'; C.H. Fulda & W.F. Schwartz,'Regulation of International Trade and Investment' Chapter 5; A.F. Lowenfeld, 'Public Controls on International Trade'; for a brief introduction of GATT law, see "The General Agreement on Tariffs and Trade" by Jackson in 'A Lawyer's guide to International Business Transactions' edited by W.S. Surrey & D. Wallace; for a complete collection of GATT documents, see 'Basic Instruments and Selected Documents' (BISD) Vol.I-IV and its annual supplements.
2. Article VI of the General Agreement, BISD Vol.II,pp.12; 55-61 UNTS; International Antidumping Code 15S/24 amended in 1979 26S/171
3. Article XI,XII, XIII
4. Article III
5. Article VII
6. Article VIII
7. Article IX
8. Article X
9. Article XVI
10. Article VI
11. For discussion of non-tariff trade barriers, see R.E. Balwin, 'Nontariff Distortion of International Trade'; G. Curzon & V. Curzon, 'Hidden Barriers to International Trade', and 'Global Assult on Non-tariff Trade Barriers'
12. BISD 26S/56
13. BISD 26S/116, 151
14. BISD 26S/154
15. BISD 26S/8
16. BISD 26S/33
17. Arrangement Regarding International Trade in Textile BISD 21S/3; Protocol Extending the Arrangement Regarding Trade in Textiles BISD 24S/5
18. see Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries, BISD 26S/203
19. BISD 26S/91
20. BISD 26S/84
21. U.S. Commerce Department, 'Task Force on Services and Multilateral Trade Negotiations, United States Services Industries in World Markets; Current Problems and Future Policy Development'. The Brandt Report also suggested that trade in services be included in GATT negotiations. For a comprehensive study of the so-called "invisible" trade, see B. Griffiths, 'Invisible Barriers to Invisible Trade'. For a specific study on trade in insurance, see R.L. Carter and G.M. Dickinson, 'Barriers to Trade in Insurance'
22. There are three difficulties, as suggested by G. Griffiths, in having invisible trade under GATT-style multilateral control: (1) that of reducing a heteogenous set of barriers to a manageable number, while at the same time ensuring that major problems are being

examined; (2) devising a system for negotiation; and (3) ensuring that agreements are in fact enforced, Griffith, pp.93-4. In addition, one might confront with the difficulty in linking the notion of tariff with barriers in invisible trade. The only possible argument is that barriers in invisible trade would have adverse effects on trade in goods and the benefits resulting from tariff reduction would be impaired.
23. BISD 18S/24
24. Article XXI
25. Article XII, XIII, XIV, XV and XVIII
26. Article XXIV
27. Article XX
28. Article A-F, Article I para. 2(A), 2(B)(b)
29. Article III
30. for GATT dispute settlement procedures and alternatives for GATT reform, see R.E. Hudec, 'Adjudication of International Trade Disputes'
31. Major sources of materials regarding the IMF for lawyers are: A.F. Lowenfeld, 'The International Monetary Fund', J.H. Jackson, 'International Economic Relations', Chapter 13, L. Larzar, 'Transnational Economic and Monetary Law, Transactions and Contracts' Book 3. For general interest, see R.Solomon, 'The International Monetary System 1945-1976, An Insider's View'
32. Article IV Sec. 4(a)
33. Article IV Sec. 4(b)
34. Article IV Sec. 5
35. M.W. Keran & M. Penzer, 'Gold As a Private Hedge against Inflation', Business Review, Federal Reserve Bank of San Francisco, Winter 1975-76
36. Decision Implementing Smithonian Agreement, Decision No. 3463-(71/126) December 18, 1971
37. R.E. Aliber, 'Stabilizing World Monetary Arrangements', pp. 22-3
38. Joint Declaration issued at Rambouillet Nov. 17, 1975, 14,4 IMF Survey 350 (Nov. 24, 1975), 11 Weekly Comp. Pres. Docs. 1292 (1975); for a brief history of the move to floating exchange rate system and the attitudes of industrialized countries, see Lowenfeld, 'International Monetary Fund', pp.203-6
39. Article IV Sec. 4, Second Amendament of Articles of Agreement of International Monetary Fund (1976); under the amendament, the Fund may permit "the introduction of a widespread system of exchange arrangements on stable but adjustable par value" by an eighty-five per cent majority of the total voting power.
40. Article VIII, Second Amendament
41. Lowenfeld, p.101-3, see note 31
42. Aliber, p.23, see note 37
43. Ibid, p.34
44. For general backgrounds and historical development of the North-Sounth problem, see L.Anell and B. Nygren, 'The Developing Countries and the World Economic Order'; L. Lazar, 'Transnational Economic and Monetary Law, Transactions and Contracts' Book 4, Chapter I, II, and Book I; the Brandt Report; for a critical view of the dialogue, see W.M. Corden 'The NIEO Proposals: A Cool Look'.

Chapter II: Trade Liberalism v. Interventionism

(A) Fundamentals of Free Trade Theory --- A Classic View

The key of the theory of free trade is the law of comparative advantage which means whether a country is absolutely strong or absolutely weak, it can maximize the power avialable to it by concentrating on those activities in which it is relatively more powerful and hiring the services of specialists in those activities in which it is weaker. Through international trade, the scope for the specialization of labour and for achieving economies of scale by the enlargement of markets can be broadened. Thus, the total volume of world output would increase and there would be more goods for consumption at lower prices.

The sources of comparative advantage, as implied in the Ricardian model of comparative cost, are differences in natural climatic conditions.*1 A more advanced view is presented by the relative-factor—availability theory, which was established by Heckscher, refined by Ohlin, and developed further by Samuelson.*2 According to this theory, the sources of comparative advantage are the differences in relative "endowments" of capital and labour, differences in capital-to-labour ratios, and differences in national wealth and affluence.

Both the Ricardian and the Heckscher-Ohlin-Samuelson models carry the implicit assumption that involvement in international trade entails the enjoyment of economic benefits from efficient resource utilization with little or no cost in terms of serious disturbance to men's livehood and economic and social lives. This assumption is constructed on the basis that the adjustment process of resource allocation is slow and smooth. The validity of the basis is possible in the Ricardian model because comparative advantages are fixed by nature; and in the Heckscher-Ohlin-Samuelson model, because changes associated with accumulation of capital per se is likely to be slow, regular and predictable.*3 Therefore, with few exceptions,*4 interventionist economic policies could do little or only have the effects of reducing real incomes and economies. This assumption is subject to modifications as a result of the emergence of new sources of comparative advantage in modern economy. These new sources not only affect the existing patterns of comparative advantage but the smoothness and speed of the adjustment process, and therefore provide possible bases for arguments for intervention. In the following, these new sources of, and changes in the patterns of, comparative advantage, and various arguments for intervention will be discussed.

(B) New Sources and Changes in Patterns of Comparative Advantages

(1) Technology

The modern theory of international trade attributes the direction and product composition of commerce among nations to a variety of factors.*5 Among others, the nature of product cycle of the traded commodity, which tends to alter the optimum location of production as a product moves through various stages of invention, development, maturity, and obsolenscence, is directly related to technological innovations. At the early stage of the product cycle of a new commodity, there involve a large amount of capital investment and much skilled labour. In the process of development, more of these are needed to test the product in home and foreign markets and to generalize consumer acceptance. As the product has reached its maturity and been standardized, it is possible to allow mass production which requires lesser labour skills and may be no more capital-intensive. Hence, the location of production may start to shift to where labour costs are relatively lower. The technology involved can be moved from one location to another and accumulated in the new location fairly quickly on a large scale, although it took a much longer period of time to develop such technology. On the other hand, the process of decumulation and conversion in the country which first invented the technology is expensive and socially painful. This is because technological knowledge is embodied in the skills and knowledge of human being, and the lengthened life expectancy and the social systems of developed countries prevent the adaptation to new skills by their labour.*6

The mobility in transplantation, rapidity in accumulation and difficulty in decumulation and conversion have ensued two consequences. First, countries where labour costs are low gain the comparative advantage in the production of those products that have reached their maturity stages, and producers in developed countries are outcompeted. Industrially advanced countries only retain comparative advantage in the employment of those technologies which will be profitable only when general affluence and educational levels have been raised sufficiently.*7 Second, industrial countries are confronted with the difficulty in adjusting from declining to new industries. The rate of "structural unemployment" has been increasing and the time period of "frictional unemployment" lengthening. The labour-saving nature of current technology development, and the lack of new dynamic industries capable of magnetizing those unemployed in other industries further worsen the unemployment problem.

(2) Energy Cost

The sudden increase in oil prices from 1973 onwards has greatly affected the existing patterns of comparative advantage. The pattern of demand was shifted to energy-saving products and the pattern of production was changed from energy-intensive to labour-intensive, when the substitution of labour for energy is possible. The effects of high energy cost on employment could be offset by the use of labour to substitute oil, if wages were flexible downwards.*8 However, the prevalence of wage rigidity in industrial countries makes such alternative infeasible and creates structural unemployment problems.

(3) Trade Unionism

Strong bargaining power of trade unions in industrialized countries often results in interruption of production and wage rigidity. A country with more harmonious industrial relations or more competent in eliminating wage rigidity may maintain comparative advantage in production. Inflexible wage rates resulting from strong bargaining power can not be considered a kind of market distortion because the society's gain from its preference for strong trade unions may offset the high labour cost as a result. If the strength of the trade union exceeds what is acceptable to the society, it may turn out to be a source of distortion. The most appropriate way to correct such a distortion is through legislation or political means to reflect the real social needs. The second chioce, when the legislative or political means fail, is to adopt flexible exchange rates. In the case that the distortion only exist in a specific industry, a subsidy to compensate would be appropriate.*9

(4) Environmental Pollution

Environmental issues have been gradually integrated into the theory of comparative advantage. Through the supply side, environmental assimilative capacity can be considered a factor of production and therefore a determinant of comparative advantage.*10 Countries with greater environmental assimilative capacity will need to devote relatively fewer resources to pollution control than those that are less fortunate. Through the demand side, demand for environmental quality will determine to what extent resources must be devoted to pollution control.*11 Disparities in national pollution control standards would also affect the relative costs of production and therefore competitiveness among trading nations. Producers in a country imposing lower pollution control standards may gain comparative advantages and the society as a whole bears more of those costs not integrated than a society with a higher pollution control standards. The advantage through demand side will disappear when there are internationally agreed standards for pollution control. Internalization of pollution control costs can be attained by following the "polluter pays" principle (PPP). According to the PPP, import restrictions and subsidies intended to neutralize the resultant competitive pressure should not be allowed. There will be more detailed discussions concerning the PPP in Chapter I Part Two.

(C) Arguments for Government Intervention

We have observed the classic theory of international trade and the new sources of comparative advantage as well as the resulting changes in the pattern of comparative advantage which in turn created new needs for intervention. In the following, both traditional and newly emerged arguments for intervention will be examined. It is worth-noting that some of them are not necessarily valid without qualification and some others may be even without validity at all.

(1) National Security and Political Stability

Protection for reasons of national security has a long history. Arguments for the maintenance of arms production is superfluous as a state usually enjoys a monopoly of national defense.*12 However, the argument is valid in allowing discretionary government procurement in the case that a state does not monopolize the production.

The rapidity and the inherent nature of technological changes, together with the wage rigidity resulting from strong bargaining power of trade unions, has shifted comparative advantages in the production of technological commodities having reached their maturity stages to developing countries. The substitution of labour for energy as a result of sudden and drastic increases in oil prices gave comparative advantage to those countries with lower labour costs. All of these are directed to the worsening unemployment problem of developed countries who appear unable to keep the adjustment process in pace with the rapid secular changes. The unemployment problem in turn arouses unrest and political instability. Government intervention is thus necessary to slow down foreign penetration and gain time for adjustment.

(2) National Policies and Goals

National policies aimed at self-sufficiency, equal distribution of income among all sectors or regional balance often present strong arguments for intervention. The most pronounced cases in this regard are agricultural protection and regional aids. Although the importance of these interventions is generally recognized,their effects on trade are one of the major sources of international conflicts. The difficulty in reconciling this standard case of international order v. domestic interest lies in the definition of the extent to which external effects of an intervention can be allowed.

Trade rules in this regard can only be laid down in an abstract form, and their actual application may appear extremely difficult.

(3) Market Distortion

The classic free trade theory is built on the assumption that there is perfect competition in the marketplace, and market forces can fully direct allocation of resources efficiently. However, there always exist market rigidities, i.e. supply and demand do not react sufficiently to price inducements. A general proposition is that distortions should be tackled as closely as possible to their sources.*13 Therefore, non-tariff intervention is almost invariably preferable to tariffs in removing distortions. The two exceptions to this general proposition are (1) the case of "wrong direction" of trade and (2) the case of infant industry.*14

(a) Domestic Market Distortion

(i) Commodity Market Distortion

An imperfectly competitive market structure may cause the market price of a commodity to exceed its opportunity cost. The best means to correct such distortion would be antitrust legislation. However, antitrust practices may not fully correct the distortion, because of the fear that relatively more stringent antitrust policies than those of other countries may hurt the competitiveness of domestic producers. A government subsidy scheme can be a supplementary mechanism to correct the residual effects of imperfect competition by cutting the market prices and increasing the output of the commodity in question.*15 On the other hand, government-induced divergence such as distortions resulting from government policies to encourage the formation of large firms no matter whether they are efficient or not should be considered as a distortion.

Government intervention is also necessary to remove the divergence between private and social marginal costs as a result of externalities in either consumption or production.*16 Taxes should be used to counteract the effects of external disconomies, such as the imposition of taxes on the use of highly polluting products or on producers of goods the production of which results in heavy pollution. Subsidies are appropriate means to compensate for external economies.

(ii) Factor Market Distortion

Factor price rigidity results in national outputs being less than optimal as factors remained unemployed at existing factor prices. When a factor, whether labour or capital, is overpriced in a particular industry, a subsidy on its use in that industry is necessary. If price rigidity exists in all industries, a system of flexible exchange rate is the appropriate means.*17

Factor immobility, mainly caused by foreign import competition, especially labour immobility, only imposes economic costs on a society when it is accompanied by factor price rigidity.*18 Adjustment assistance programmes and regional development aids are sound mechanisms to correct the distortion. However, given the danger of abuse, some economists argue that lump-sum subsidies are preferable than production subsidies, because they are less of non-tariff distortion in the long run and they encourage exit from a declining industry.*19

(iii) Infant Industry

Infant industries, which in their initial stages of development, cannot compete on equal terms in world markets with well-established suppliers who enjoys the accrued benefits of economies of scale in production. Non-tariff intervention, especially subsidies, are appropriate measures in nurturing infant industries,*20 because an infant industry will never mature and face foreign competition under the protection of tariffs.*21 The criterion in assessing the validity of an argument for intervention in a specific case is whether the gain from protection will be sufficient to wipe out the cost to the society rather than whether the comparative advantage will eventually appear.*22 This is because intervention in one industry which has either high forward or backward linkage effects may generate externalities which are essential for other industries to reach their take-off stages. An intervention should be aimed as closely as possible at the activity within the industry which generates such externalities.*23

(b) Foreign Market Distortion

(i) Otimum Tariff

Imposition of an optimum tariff by an importing country having monopolistic buying power may have the effect of raising the welfare of the country above what it could be under free trade. The rationale goes like this: tariffs restrict imports to such an extent that an excess supply is generated on the world market. World market prices thus fall in order to clear the market and the international terms of trade shift in favor of the tariff-levying country. Although optimum tariffs maximize the welfare of the individual country, they do not do so for the world as a whole. Moreover, the possible retaliation by other countries may make the volume of trade fall, and all countries lose.*24

(ii) Dumping and Subsidy

Dumping is a practice of price discrimination. It is often made possible by the dumper's monopolistic position in his home market and high tariffs of the exporting country to prevent the inflow of the goods having the characteristics of those of the dumped goods. Since the source of distortion in the case of dumping lies in the market imperfection in the exporting country, the proper remedy is antitrust practice or other measures to restore competition in the domestic market of the exporting country. Imposition of countermeasures by an importing country, except in few cases, would create further distortion.

In the case of subsidy, the distortion lies in the extra advantage that producers have from government assistance. However, in many cases, subsidies are used as corrective measures to remove existing market distortion. The proper measure to eliminate a distortion resulting from the use of a subsidy is to remove the subsidy in question. Imposition of countermeasure by an importing country, though can partially eliminate the effect of a subsidy, may prove to be inappropriate and sometimes create more distortions.

There will be detailed discussion on the economics of dumping and subsidy in Part Two as these practices are two of the main concerns of this thesis.

(iii) Foreign Exchange Market

Under a fixed exchange rate regime, government intervention is needed to maintain the par value of a currency. An uniform import-levy/ export-subsidy scheme having the same effects as adjustment in exchange rates is a mechanism that can be used to correct a short-term balance of payment disequlibrium.*25 The move to a regime of flexible exchange rates should greatly eliminate the need for intervention in this regard.

(4) Protection As An Alternative for Maintaining Balance of Payments

--- the CEPG Argument *28

In 1975, a group of economists at the University of Cambridge (the Cambridge Economic Policy Group, CEPG) advanced an argument for the imposition of general import restrictions to prevent the balance of payments of the U.K. from worsening. They also argued that the use of exchange rate adjustment to achieve the same aim would be dangerously inflationary. In 1978, the CEPG extended its argument to any country who encountered balance of payments deficits and suffered from masss unemployment. The CEPG argument is a subtle one, but only its preference for import restriction over exchange rate adjustment will be examined here. First, the CEPG maintains that the income loss following devaluation will considerably exceed the welfare loss associated with import restrictions. This assertion could be invalidated by taking into account the longer time-period over which import controls persist, and by discounting the future cost to the present. Secondly, the CEPG argues that a cut in living standard inevitably follows devaluation, because of the inflationary rise in import prices. However, the same can also be seen when either quantitative import restriction or tariffs are imposed. Thirdly, according to the CEPG plan, unemployment can be alleviated by the expansion of import-substitute industries. However, exchange rate adjustments, which improve not only import - substitute but export-oriented industries are certainly preferable than import restriction. Fourthly, protection on the scale of import control as recommended by the CEPG contravenes the U.K.'s obligation under the GATT, the IMF, the Rome Treaty, and towards other OECD countries and invites retaliation.

CONCLUSION

This chapter has examined the classic free trade theory and the emergence of new sources as well as changes in the pattern of comparative advantage. These events inject various new needs for government intervention. While the argument for national defense is superflous when a government enjoys a monopoly in arms production, there is a valid case for political instability associated with the mass unemployment in the secular change. The pursuit of national goals should be allowed if its external effects on international trade do not exceed the limits set by international agreements. Intervention is necessary in correcting market distortions. In the case of commodity market inperfection, subsidies can be used to supplement the deficiency of legal mechanism and government intervention, either in the form of subsidy or tax, is necessary to remove the divergence between private and social marginal costs. Subsidies are also the right mechanism to deal with factor price rigidity and factor immobility, while changes in the exchange rate provide an alternative when distortion exists in all industries. Non-tariff measures are preferred in nurturing infant industries, and the criterion in assessing the validity of an intervention is whether the gain from intervention will be sufficient to wipe out the cost to the society. When distortions exist in foreign markets, the imposition of optimum tariff would result in losses in world welfare and invites retaliations. Counteractions against dumped and subsidized imports are inappropriate means to correct market distortions. The move towards a managed floating exchange rate system greatly eliminated the need for intervention to maintain the par values of national currencies. The CEPG's preference for general import restrictions to improve balance of payments position is invalidated by various counterarguments.

Footnotes (Part Two, Chapter II)

1. D. Ricardo, 'Principles of Political Economy and Taxation', Chapter VIII
2. B. Ohlin, 'International and Interregional Trade'; P.A. Smuelson, "International Factor Price Equalization Once Again", E.J. June 1949; H.G. Johnson, "Comparative Costs and Commercial Policy" in 'Money, Trade and Economic Growth'.
3. H.G. Johnson, Forewords to the 'Trade Effects of Public Subsidies to Private Enterprises' by G. Denton, S. O'Cleireacan and S.Ash, pp.xxv
4. The exceptions allowed by the classic theory are (i) the "terms of trade" or "exploitation of monopoly power" argument for protection and (ii) the "infant industry" argument for protection. These two exceptions will be discussed in the latter part of this chapter.
5. These factors are (i) international differences in the availability of productive factors, (ii) international differences in factor productivity, (iii) international differences in the quality of productive factors, (iv) international differences in economies of scale and hence in the average size of production units, (v) international differences in demand patterns, and similarities or dissimilarities of relative preferences, and (vi) the nature of the "product cycle" of traded commodities.
6. H.G. Johnson, see note 3, pp. xxvi-xxviii. The difficulty in decumulation and conversion is due to two factors: (i) the lengthening of life expectancy and declining capacity to adapt to learn new skills and habits after reaching adult maturity, and (ii) under the social system of advanced countries, every one is expected to concentrate on the career chosen in his early adulthood. For more elaborte discussion regarding technological changes, see Johnson, 'Technology and Economic Interdependence'
7. Ibid
8. W.M. Corden, "Framework for Analyzing the Implications of the Rise of Oil Prices" in 'The Economics of the Oil Crisis' edited by T.M. Rybczynski, pp.19-29
9. G. Denton and S. O'Cleireacain, 'Subsidy Issues in International Commerce', pp.11-2
10. I. Walter, 'International Economics of Pollution', p .79
11. Ibid. p.87
12. D. Greenaway and C. Milner, 'Protectionism Again...' p.19
13. J. Bhagwati and V.K. Ramaswami, "Domestic Distortions, Tariffs and Theory of Optimum Subsidy", J. of Political Economy, Feb 1963, p. 49
14. Wrong direction of trade means the importing of a commodity in which a country really has a comparative advantage which is not immediately obvious due to distortion. Issues related to infant industry will be discussed later in the text. In these two cases, it is not clear whether the imposition of tariffs would raise or lower national welfare. Denton & O'Cleireacain, see note 9, p.8
15. Denton & O'Cleireacain, see note 9, p.9
16. Ibid, p.10
17. Ibid
18. Ibid, pp.11-2
19. R.E. Baldwin, 'Nontariff Distortions of International Trade', p .125
20. Denton & O'Cleireacain, see note 9, p.13
21. Greenaway & Milner, see note 12, p. 24
22. Ibid

23. G. Denton, S. O'Cleireacan, and S.Ash, 'Trade Effects of Public Subsidies to Private Enterprises', pp.15-6
24. Greenaway and Milner, see note 12, pp.15-6
25. Baldwin, see note 19, pp.47-8
26. Mundell, "Flexible Exchange Rates and Employment Policy", Cambridge J. of Economic Policy Series (Nov. 1961); Cripps and Godley, "Control of Imports As A Means to Full Employment and the Expansion of World Trade", Cambridge J. of Economics (Sep. 1978); for arguments against CEPG, see H. Corbert et al., 'On How to Cope with Britain's Trade Position'; W.M. Corden, I.M. Little, and M.F.G. Scott, 'Import Control versus Devaluation and Britain's Economic Prospects', and 'The Case against General Import Restrictions'

Chapter III: Current Trade Conflicts

This chapter examines current conflicts between trading nations as a result of the structural changes and current recession. The emphases are the various use of non-tariff import restrictions, subsidies, the role of law in the process of resolving the conflicts and the legal chaos resulting from those irreconcilable trade conflicts.

(A) Trade Conflicts between Developed Countries

(1) Border Tax Adjustment

A border tax adjustment is a "process by which imports are subject to and exports are exempted from internal taxation whenever this process takes place".*1 However, such adjustment most often occures at the border. The purpose of making a border tax adjustment is to equalize the conditions of competition between domestic and foreign producers and so permit comparative cost to govern the trade pattern. Border tax adjustment is different from a border tax in that the latter is a tax imposed on the goods crossing international frontiers such as a tariff, and hence restricts the volume of trade below what is desired by the principle of comparative advantage.

Conflicts arising from border tax adjustments started from the EEC's move towards harmonization of internal taxes of member countries. Each member under the EEC harmonization scheme was to replace its turnover tax by a value-added tax. A turnover tax, also called a cascade tax, is a tax levied as a proportion of the price of a commodity on each sale in the distribution chain, while a VAT is applied at each point of exchange of goods or services but the tax base at each stage is only the value added by the sellers. Under the turnover tax system it is difficult to calculate the tax precisely, and border tax adjustments made within the EEC were usually lower than the permissible level under the GATT rule which allows full rebates for indirect taxes.*3 The shift to a VAT system,under which accurate calculation is possible, would benefit the EEC exports by granting them a larger amount of rebate. This was considered by the U.S. as a subsidy. Moreover, the U.S. questioned whether a VAT was an indirect tax which under the GATT rule can be fully refunded upon exportation. A VAT is regarded by some as a hybrid of indirect and direct taxes, because a VAT though ultimately borne by consumers is levied on producers. Thirdly, the U.S. challenged the soundness of the GATT rule which allows full refund of indirect tax, because indirect taxes are not necessarily fully shifted to consumers and allowing full refund would amount to granting subsidies to exporters. Countries like the U.S. primarily rely on direct taxes which under the GATT law are not allowed to be refunded would be in a disadvantageous position, because direct taxes are also likely to be shifted to consumers. These issues were brought to the GATT in 1970 and members of the Working Parties were unable to reach a consensus.*4

The tax issue was also contested in domestic context. U.S. steel producers urged the U.S. Treasury to impose countervailing duties on European steel imports because they were exempted from VATs and the market conditions in the EEC did not permit complete shifting of VATs. The Treasury, after a period of hesitation, in 1975 rejected the petition by the U.S. steel industry on the ground that it did not regard refund or exemption of VATs as a subsidy practice.*5 When the tax issue was brought to the court in the <u>Zenith Radio Corporation v. United States</u> *6 regarding refund of commodity taxes by the Japanese Governments, the U.S. Supreme court refused to intervene in the

Treasury's decision that full refund of commodity tax contained no element of subsidy.

Another focus of the disputes arising from border tax adjustment concerns the levy of taxes on corporations. The issue in point was the U.S. tax deferral system, known as Domestic International Sales Corporations.*7 Under the system, an U.S. exporter can set up a DISC and one half of the DISC's earnings would not be taxed until certain events occur. As revealed in the legislative history of the Tax Reform Act of 1976, the DISC programmes had resulted in a significant increase in the U.S. exports.*8 The DISC was alleged by the EEC as an export subsidy practice, because exporters benefited from not paying the interest of the tax normally levied for late or deferred payment. The U.S. argued that the DISC was intended to offset the effect of the tax practices of some European countries, namely, France, Belgium, and the Netherlands. The European tax practice in dispute is the territoriality principle adopted by these countries. According to the principle, national companies are liable to corporation tax solely in respect of profits made by enterprises operating within the territory of the taxing country or in respect of profits taxable by the country under an international double taxation agreement. Since the enterprise's profits made from activities in foreign countries are exempted from corporation tax of its base country, the application of the principle was accused by the U.S. as an export subsidy practice.

Both the DISC and the territoriality principle were found by a GATT investigation panel to be export subsidies.*9 The disputes were settled by an agreement between the parties that governments on both sides were allowed to tax their oversea corporations as they saw fit.

(b) Export Credit and Export Guarantee

The change from the seller's market to the buyer's market after the post-second war reconstruction enabled buyers to stipulate the payment terms, which tended to shift from cash to credit and from short to longer credit periods.*10 Export credit as an element of competitiveness is particularly salient in the exportation of capital goods. This is due to the increasing degree of homogeneity of export products of the industrialized countries. Moreover, the size of transaction in capital goods and the status of the buyers , mostly developing countries, mean that they can only be sold on credit. Most importantly, governments are competiting with one another in subsidizing export credit, because capital goods, such as construction equipments, aircrafts, textile machinery, and electrical machinery, often have great repercussions on balance of payments, employment, or the survival of strategical industries, and are more vulnerable to changes in recession. There is also the problem of mixed credit,i.e. a financial package mingling commercial credit with concessional aid.

The first international effort to control competitive subsidization in export credit was an understanding reached in 1953 within the framework of the Berne Union (International Union of Credit and Investment Insurers), which was set up to coordinate the practices of various export-credit agencies. The understanding permits any member to adopt the most liberal term offered by other members. The Burne Union proved to be ineffective because (1) it is non-governmental organization, (2) it only deals with practices of export credit insurers, and (3) the understanding has no binding legal force.*11 In 1962, EEC member countries reached an agreement according to which export credit of more than five years, that were covered by government guarantee or supported by public funds, should be subject to inter-governmental consultation.*12 A GATT working party in 1961 enlisted export quarantee programmes, at premium rates which are manifestly inadequate to cover the long term operation costs and losses, and official export credit at rates below those the government has to pay for the funds so employed, as export subsidies.*13 The 1979 MTN Subsidy/ Countervailing Duty Code also takes the same position.*14

The most important organization in harmonizing export credit policies of industrial countries is the Organization for Economic Cooperation and Development, (OECD). The OECD permanent Group on Export Credit Guarantees, established in 1963 by the OECD Trade Committee, from mid-1960s has made possible an agreement and two understandings in regard to transactions in shipbuilding, large jet aircrafts and ground satellite communication stations. In 1976, except a few countries, OECD member countries acceded to a Consensus which sets out minimum cash payments and interest rates, and maximum repayment terms, as well as procedures to notify other countries when a country proposes to exceed the guidelines, or to offer mixed credit with a grant element of less than 20 per cent. In 1978, the Arrangement on Guidelines for Officially Supported Export Credits was reached. The Arrangement is more comprehensive than the Consensus and differs from the Consensus in that the latter is a collection of seperate declarations made at different times and susceptible to individual interpretation, whereas the Arrangement is a single uniform document to which all the members of the OECD Export Credit Group subscribed from the outset.*15

Although the Arrangement has achieved more orderly competition, the inflexibility of the guidelines prevented their adjusting in line with changes in international economy. The rates provided are far below market rates as the cost of export credit has been increasing. Moreover, an uniform minimum rate applying to all countries may impinge on official support of export credit from country to country unevenly. Countries with low domestic interest rates and strong currencies, like Japan, complained that those countries with high interest rates were providing large subsidies to enable their exporters to quote the minimum rates, whereas they had to offer rates above their domestic rates. On the other hand, export credit agencies of those countries with high interest rates, such as the U.S., Canada and Britain, would face with a large amount of deficits, if they were to meet international competition at an uniform rate much lower than their market rates. The issue would become even more complicated, when the fact that government interventions in capital markets by controlling interest rates have become common practices as a part of their macro-economic policies is taken into account.

To pacify the soaring export credit war, the Wallen report, named after the Swedish chairman of the OECD Commission on export Credit, Mr. Axel Wallen, proposed three alternatives: (1) each country could have different export credit interest rates, linked to its domestic interest rates (the differentiated rate system, DRS), (2) different interest rates for each country offering credit but with a ceiling for countries with problems, and (3) the same level of interest rates for all countries, but linked to the market rates, worked out on a weighted average (the uniform moving matrix system, UMM). The U.S. who insisted export credit reflect market rates more closely would like to see the first adopted and was prepared to accept the third.

However, given the EEC's intransigence, only a small rise was possible. After a long period of negotiation, all the OECD nations, except Japan, finally agreed in Paris that the interest rates should be increased by between 2.25 and 2.50 per cent.*16 The U.S. was compensated by the extention of maturity of loans to offset the heavier use of subsidies on the European side. After a short period of hesitation, Japan approved the compromised set of minimum interest rates.

(c) Trade in Temporate-Zone Agricultural Products

Agricultural protection presents one of the most complicated issues in international trade. Agriculture provides an essential human need, employs hundreds of thousands of small businessmen in rural ares where other employment opportunities are scarce, and is in a tendency to stress the adoption of labour-saving technology which requires a significant resource adjustment to alleviate.*17 Government intervention is though necessary to attain self-sufficiency, to secure supply or to stablize prices and therefore producers' incomes, and to ease the farming population over the changes and adjustment.

In most developed countries, the allocation of resources to agriculture is taken out of the control of the market mechanism and placed in the hands of governments. The U.S. agricultural policies are aimed at protecting the agricultural sector by means as close as possible to the market mechanism. This is done by demand expansion and supply control.*18 Demand expansion is stimulated by a food stamp programme at home to increase consumption by the urban poor and by active promotion of both commercial and concessionary exports. Voluntary production limitation is the means of supply control.

Direct payments are made for voluntary withdrawal of land from production as income supplements when the market prices fall below an agreed target price. The selling prices of farm commodities are the equilibrium prices established by the increased demand and limited supply. The scheme is different from the previous one under which the Commodity Credit Corporation was to buy unwanted commodities in order to maintain the market price at high levels. In addition, quotas are imposed on various agricultural imports either through legislations or through bilateral agreements.

The EEC Common Agricultural Policy (CAP) is the most elaborate of all systems of protection for agriculture. Every year the prices of the main agricultural commodities produced in the EEC are agreed by the Council of Ministers. If the market prices fall below the agreed level, the Community would intervene in the market by buying necessary amount of commodities to support the prices. The large stocks that the EEC accumulates are disposed of by an export subsidy or converted to other products not in oversupply. Since most of the EEC commodity prices are fixed above world prices, it is necessary to control imports. Imported food products are taxed sufficiently to bring their market prices up to the support prices, or the market prices of the EEC, if they are higher than the support prices. The CAP also has a safeguard clause for some commodities, allowing appropriate measures to be taken if imports cause, or threaten to cause, grave disturbances in members' markets which might interfere with the basic objectives of the CAP.[*19] On the other hand, if the EEC prices are below world prices, export levies will be imposed to discourage the shipment of EEC produce to more lucrative world markets. The EEC is unable to increase demand by pursuing such policies as the U.S. food stamps.

This is because the EEC intervention agencies are already buying the surpluses, so that the effective demand within the EEC has been raised to the highest possibility. Subsidized sales of the stockpiles will widen the gap between supply and demand even further. Moreover, the CAP lacks an effective mechanism to control production. Being unable to increase demand within the Community and to control over-production, the EEC has to allocate enormous funds to subsidize exports of stockpiles. As a result, many traditional exporting countries of food products are under the threat from the EEC subsidized exports.

In controlling the external effects of domestic agricultural policies, one has to draw attention to three issues: (1) stabilization of international markets and prices, (2) access to supplies and for exports, and (3) the need of some developing countries for food aids or concessional sales. With these considerations and the strong political needs for supporting the agricultural sector, it is unrealistic and impossible to expect full liberalization of agricultural trade.

The Dillon and Kennedy rounds of the GATT negotiation had greatly reduced agricultural tariffs, which although significant for some products have not been the main obstacles to international trade in temperate-zone products. The issues for the Tokyo Round were those of non-tariff distortions and of safeguard procedures. The impact of high prices on inflation and the tendency for government spending to be more tightly controlled improved the political atomosphere for the Tokyo Round negotiations.*20 The achievement of the Tokyo Round with respect to agricultural trade is more significant than that of previous rounds. Among the MTN codes, the Subsidy/ Countervailing

Duty Code and the Standard Code are the most important ones to agricultural trade. The Subsidy/ Countervailing Duty Code does not prohibit subsidies in agricultural trade, but an export subsidy shall not be "in a manner which results in the signatory granting such subsidy having a more than equitable share of world export trade ...".*21 Although the Standard Code does not seek to set product standards or to prescribe specific guidelines for setting the standards, it makes the standard-setting process fairer and more accessible to the interested parties and encourages the establishment of international standards. In addition to these codes regarding the use of various non-tariff trade barriers, the Tokyo Round also produced several agreements regarding trade in specific agricultural products.

Meats

The major problem in the meat market has arisen from import restrictions, usually of quantitative nature. These quantitative restrictions in turn have created considerable uncertainty for exporters. The Bovine Meat Agreement*22 does not provide any substantive rules in controlling the use of import restrictions which is to be dealt with under the various provisions of the General Agreement regarding the use of trade barriers. In stead, the Agreement is aimed at the coordination of production and trade policies of signatories and therefore reducing conflicts. An International Meat Council is set up to monitor and assess the overall situation of the world market.*23 The Council is also to provide opportunity for regular consultation on all matters affecting trade in bovine meat.*24 Through these devices, it is hoped that greater liberalization and stability of international market can be achieved.

Dairy Products

In the case of dairy product, the main problem is the EEC's inability to dispose of its huge over-production. An international agreement with a price range would have disciplinary effects on domestic subsidies. Protocols affiliated to the International Dairy Arrangement concluded in the Tokyo Round establish the minimum prices for world trade in milk powders, milk fat and cheese.*25 Although these prices are far below current levels, they serve as potential barriers to hugh export subsidies by surplus-producing countries. The International Dairy Council is set up to perform the same function as the International Meat Council in bovine meat trade. However, member countries are not obliged to follow or implement the recommendations made by the IDC, when their "trade interests are being seriously affected" as a result.*26 Special rules are also provided for concessional sales or food aids to developing countries.*27

Wheat

A multilateral agreement on wheat trade is particularly difficult, because of the relatively greater degree of substitution between several grades and kinds of wheat and other coarse grains, the existence of bilateral agreements regarding supplies of wheat and the growing politicization of wheat trade.*28 The International Wheat Agreement, which entered into force in 1971, is the latest attempt to stabilize the wheat market. As the dismantling of protection which is the concern of the GATT would inevitably influence and be influenced by arrangements for market stability, attempts were made in the Tokyo Round to incorporate the IWA into the GATT and basing on the IWA to establish a regime for trade liberalization. However, such attempts failed, and the Tokyo Round produced no special agreement for wheat trade.

The failure of the Tokyo Round in reaching an agreement on sugar trade to supplement the deficiency of the International Sugar Agreement has resulted in serious confrontation between the EEC and other sugar producing countries, among others, Australia, Brazil, and the U.S. The consequence of this confrontation may have the effects of undermining not only those efforts that have been done to regulate agricultural trade but also those to establish an orderly international trading system.*29

(d) Steel Industry

The steel industries of developed countries have undergone a few structural changes during the past two decades. First, the Japanese industry has become a dominant supplier of the world market, and threatens the steel industries of the U.S. and the EEC. Secondly, the so-called newly industrialized countries have emerged as reckoned competitors. Thirdly, the world recession since the mid-1970 has greatly enlarged the gap between world supply capacity and demand.*30 This, together with the fact that because steel production is less influenced by thechnology improvements and the products of the industrialized countries are roughly homogeneous, trade in steel products is largely affected by price, has given rise to conditions for cut-throat competition.*31 For steel is a symbol of strength and is of vital importance to the industry of a country as a whole, maintenance of an advanced steel industry has often been given priority by national governments. Trade barriers are therefore another important determinant in competition. In the observation of steel trade, one has to take into account not only tariffs, but also subsidies, dumping, internal taxes, and a variety of old and new forms of quantitative restrictions. In the following, how the U.S. and the EEC react to the steel crisis will be discussed.

One of the main causes of confrontation between the U.S. on the one hand and the EEC and Japan on the other hand in steel trade lies in the divergence between their pricing policies.*32 The U.S. steel industry has shown a tendency to set domestic prices at a level which covers both fixed and variable costs in good time and bad. Conversely, steel producers in Europe and Japan habitually practice dual pricing during recession, setting export prices at a level just adequate to cover variable cost. Moreover, the highly concentrated market structure of the U.S. has made possible oligopolistic pricing through price leadership. Facing with increased foreign imports in every recession from the early 1960s which have the effect of threatening collusive pricing, U.S. steel industry has been searching means other than price competition to preserve its market position. It first concentrated on seeking imposition of antidumping duties on foreign imports. The use of antidumping action to resist foreign competition was highlighted by the U.S. Tariff Commission's decision in 1967 in the landmark case, <u>Cast Iron Soil Pipe from Poland</u> .*33 In that case, the Commission held that to meet the injury test of an antidumping action, an injury of more than <u>de minimis</u> degree would suffice. The industry also accused foreign producers of being unfairly benefited from government assistance and has made several attempts to seek imposition of countervailing duties on foreign imports. Foreign subsidies under attack are such practices as special freight rates for domestic shipment of steel products, favourable rates on export credit or guarantee of credit, accelerated depreciation allowances on modernization of plants and the remission of the VAT by the EEC member countries.

After the failure to seek remedy under the escape clause, the national security clause, and the so-called "orderly marketing" provision of the U.S. Trade Expansion Act of 1962,*34 a bill was introduced with a view to authorizing the President to negotiate multilateral or bilateral agreements establishing quotas on steel imports when the soundness of the steel industry was threatened. Under the threat of this bill, Japan and EEC agreed to restrain their exports to the U.S. voluntarily. The VER arrangements were challenged by consumer groups about their legality.*35 The VERs ceased to be in operation in 1974, because of the worldwide boom in demand for steel products.

In order to lighten the re-emerged pressure for protection starting from 1975 as a result of recession, the Tigger Price Mechanism was introduced in antidumping administration.*36 According to the TPM, the U.S. Treasury*37 would announce a set of reference prices for steel products, which was set on the basis of the cost of the most efficient foreign producer. If there had been any foreign offer below these prices, the Treasury would have undertaken antidumping investigation. The U.S. producers in return agreed not to take legal action on their own intiatives. By using cost of production as the fair value in the determination of dumping, the TPM in effect prohibited marginal cost pricing during recession and also mixed up antidumping law with tariff law by bringing the level of import prices in line with the trigger price. The protectionist effects and the legality of the TPM have been subject to much debate and are the main concerns of disputes between the U.S. and its trading partners. The TPM was suspended for sometime but later revived in the latter part of 1980.

Steel Crisis in Europe

The main mechanism which controls the EEC steel production is the European Coal and Steel Community, established by the Treaty of Paris. The Paris Treaty is intended to "ensure the most rational distribution of production at the highest possible level of productivity, while safeguarding continuity of employment..."*38 In 1967, through the so-called Merger Treaty,*39 the management of steel trade was shifted to the EEC Commission and Council.

The Treaty of Paris is primarily concerned with a "regulated competition resulting from deliberate action and permanent arbitration" rather than the abolition of obstacles to intra-community trade.*40 The ECSC "normal" pricing system*41 which is a combination of multiple basing point system, compulsory adherence to published price lists and a prohibition of price discrimination within the Community, is in fact calculated to promote oligopolistic behavior among European producers.*42 This system is very much like the pricing practice of U.S. producers and is particularly vulnerable to import competition. The real challenge to the ECSC system came in 1976 when there was a sharp drop in demand as a result of recession. European producers, like the U.S. producers, have been the loser in the secular changes of steel trade and unable to compete with producers in the newly developed countries and Japan.

To meet the steel crisis, the Commission issued the Simonet Plan to penalize redundant investments with a view to solving the problem of low capacity utilization. The Simonet Plan was further implemented by the Davignon Plan. Under the plan, several steel products were subject to minimum prices, and some others were subject to guide or reference prices. In order to insulate the EEC market from international competition, the Commission not only increased surveillance on imports by setting up a licensing system but strengthened coordination among member states in dealing with dumping, subsidized imports and market disruption. Although the Plan was effective in disciplining prices and production to some extent, the EEC producers still suffered from strong import competition.

The second phase of the Plan was therefore directed at curbing import competition. The technique used is similar to the Trigger Price Mechanism. The Commission published a list of minimum or "basic prices" which were derived "by reference to the lowest normal costs in the supplying country or countries where there are normal conditions of competition".*43 Imports at prices below these basic prices would be deemed dumping, and provisional antidumping measures would be immediately invoked, without any prior inquiry into the question of injury. The antidumping duties, in actual practices, were not universally and permanently imposed on foreign imports. Instead, antidumping duties would not be imposed or would be lifted in exchange for an exporting country's promise to ship no more than an agreed amount into the Community and to refrain from bringing a complaint to the GATT. In addition to non-imposition or a lifting of antidumping duties, foreign producers would be permitted to bring in steel at a "penetration margin" of 7% below the ECSC guide prices, and the Community producers would be prohibited from aliging their prices with import prices. Foreign producers are therefore quaranteed of certain market share. Although import competition could be curbed, the fundamental difficulty of the industry, i.e. inadequate demand and low rates of capacity utilization, remains The issue to be dealt with in the third phase is therefore to restructure the steel industry, involving contraction, modernization and most importantly elimination of subsidies.

In an attempt to control the increasing government subsidies to steel industries, the EEC member countries in 1980 agreed to a subsidies code for steel. The code stipulates that the Commission must be informed of all aids beforehand, and would approve them only if they were geared towards "restructuring". Bailouts would be allowed only under the following conditions : (1) closures presented huge social problems, (2) the aids were for limited time, (3) they were not repeated and (4) they helped restructuring. In September 1980, the Davignon voluntary cartel plan broke down because of the continuing recession which depressed steel demand. A new plan was proposed which was put into effect at the end of October 1980 to meet the "manifest crisis" provided in Article 58 of the Paris Treaty. A system of mandatory production quota was introduced. The system was strongly opposed by Germany whose firms are efficient and some of them have restructured their plants in the 1970s to meet the recession. Germany's concern was that the new controls would guide an inefficient steel industry through the slump, allowing it to hold on to ageing, obsolescent and subsidized plants.*44 Under the pressure from Germany, the Commission then undertook to curb steel subsidies. The EEC economics ministers agreed to eliminate all national subsidies over the next few years. A timetable was also agreed. Emergency funds not immediately linked to a reduction of capacity, must cease by June 30 1982. All operational aids linked to restructuring must be eliminated by December 31 1984. The ministers also agreed to provide modest financial help for early retirement and short-time working for steel-workers.

The rise of the U.S. dallar in 1981 have led to a big assult of European subsidized steel exoports on the steel markets in the U.S. There were rapidly mounting fears among U.S. producers that the TPM is not adequate to curb import penetration. After the failure in the International Iron and Steel Institute's Conference in October 1981 to solve the issue, several antidumping and countervailing duty actions were initiated by the U.S. steel industry without resort to the TPM. In the summer of 1982, the U.S. Commerce Department rendered a positive determination of subsidy and subsequently a positive determination of injury was rendered by the International Trade Commission. Before the Commerce Department rendered its final determination, European producers agreed to an arrangement of VER limiting the amount of exports from the Community.

(e) Chemicals and Textiles

Like the steel industry, the chemical industry is also facing the problem of excess capacity and inadequate demand. The difficulty of the chemical industries of industrialized countries is not only cyclical but structural in nature. The rapid growth in the 1960s was bound to slow down as products matured and the post-OPEC economy flatered. These two factors are particularly critical to an industry that is accustomed to having its periodic problems of excess capacity problems solved by expanding demand.*45 Moreover, there is increasing competition from the OPEC petrochemical producers that have cheap local feedstocks gas, from the Eastern European producers who put more emphases on earning hard currencies than on making profits, and from third-world countries making chemicals to replace foreign imports.

The most affected are those Western European countries who are not only suffering from excess capacity, ageing plants, glutted markets, weak prices, heavy losses and endless subsidies but also from strong import penetration of U.S. exports which are benefited from government controlled energy prices. The EEC Commission responds to this import penetration with a series of antidumping actions and the constant warning that the controlled energy prices are unfair advantages. The use of antidumping duties against low price imports in the present case is specially interesting. The EEC Commission applies cost of production as normal value in determining whether imports from the U.S. are sold at prices below their normal values. However, many of the European producers are doing the same. They are struggling for volume rather than profit, thinking that things will turn out all right only if they can get through the cyclically depressed period. Since selling below cost are common practices among European producers, U.S. producers have to follow the same pricing policy in order to compete in the European markets.

Several downstream industries of the chemical industry are also in the same difficulty. This is especially true in the case of synthetic fiber. The EEC textile industry has been under the threats from third world as well as Mediteranean countries since the early 1970s. It is now also facing import competition from the U.S. where the chemical industry is benefited by the control of energy price. The EEC Commission again imposes antidumping duties on U.S. imports, applying cost of production as normal value in the determination of dumping, without regard to the fact that sales below cost are the common practices not only among U.S. exporters but among EEC producers.

(f) Auto Industry

The changing pattern of demand towards enery-saving cars enabled Japanese products to capture a large share in the world market and made possible the rapid expansion of the Japanese car industry. This Japanese expansion has greatly burdened those Northern American and Western European countries that are struggling to restructure their car industries. Moreover, the drop in demand for products of these countries has resulted in serious unemployment problems and trade imbalance. Trade unions as well as auto producers are pressing hard to take action against Japanese import competition. In the following, how the U.S. and the EEC react to Japanese import competition will be discussed.

Being unable to establish a case of dumping or subsidy, the U.S. auto producers together with auto worker unions launched a compaign against imports of Japanese cars under the escape clause of the U.S. trade legislation. They alleged that Japanese imports have seriously injured U.S. car industry and sought a presidential action to impose import restrictions. Pursuant to the U.S. Trade act of 1974, presidential actions under the escape clause are preconditioned by a positive determination of injury from the U.S. International Trade Commission.*46 In November 1980, the USITC reached a rather controversial negative determination of injury. The USITC held that the current state of the U.S. motor industry steemed less from the import menance than high petro prices, a switch in American taste from large to small cars and economic recession. In other words, the Commission felt that import competition did not constitute "a substantial cause of serious injury" and therefore the causal connection between the two was not strong enough. Failing to establish a case under the escape clause, U.S car industry then turned to another alternative, namely, to negotiate with Japanese producers a voluntary export restraint. The legality of the VER was challenged by U.S. consumer groups with regard to steel imports. In Consumers Union of U.S. Inc. v. Kissinger *47, the U.S. Court of Appeals affirmed the district court's declaration that both the U.S. Expansion Act and Sherman Act did not prohibit the President from "negotiating in any manner with private foreign companies as to commercial matters". However, the declaration that "the executive has no authority under the Constitution or acts of Congress to exempt the Voluntary Export Restraint Arrangements on steel from the antitrust laws and that such arrangement are not exempted..." was vacated.*48 Even though the declaration with respect to antitrust law was vacated, it is still possible for negotiation of a VER to constitute an antitrust offence. The Sherman Act condemns any conspiracy or agreement to restrain competition in the U.S. market. In order to avoid being involved in the troublesome antitrust litigtion, the only alternative is to seek an immunity for all parties concerned is a congressional action to authorize the President to negotiate car import restrictions with Japan and other countries. In December 1980, a bill enpowering the President to negotiate was easily passed. An agreement was eventually reached according to which Japan was to limit its car exports to the U.S. voluntarily .

The U.S.-Japan agreement irritated the EEC whose car industry is in a declining state and heavily subsidized by the governments. The EEC claimed that it was damaged by the bilateral dealing, because there had been no adequate consultation with the EEC. This showed the most disregard of the interest of the EEC, because it undermined the progress made between the U.S. and the EEC towards developing a coordinated political attempt to turn back the tide of imports of sensitive products from Japan. Moreover, the agreement could bring more pressure on the EEC markets as there would be diversion of sales to these markets. The EEC therefore sought to gain a pledge from Japan that it would restrain car exports to the EEC in lines with its restraint agreement with the U.S. However, the EEC member countries were unable to agree on the nature of any voluntary undertaking that might be secured from Japan. This is because many member countries were already protected by national measures, or voluntary export restraint agreements and were reluctant to give up their sovereign rights in this area.*49 Rather than facing a concerted EEC, Japan settled the dispute with individual countries one by one with a series of voluntary export restraint agreements.

(B) Trade Conflicts Between Developed and Developing Countries

Developing countries are also affected by the current economic crisis, partly due to the reactions of developed countries to the crisis. The recession-induced protectionism not only hurt developed but also developing countries. Protectionist devices such as "orderly marketing arrangements" and "voluntary export restraints" are directed largely against labour-intensive products and the whole process of economic development of developing countries is severely affected by restricted access for many "first stage" manufacturing products. Moreover, the tendency among developed countries to cut government spending has greatly reduced the amount of aid to developing countries. In addition, the drastic increase in oil prices results in balance of payments difficulties in the net oil-importing developing countries, particularly those of low income countries and those of middle income countries who are unable to expand their exports of manufactures in recession to cover their oil bills.

Although most developed countries grant preferential tariff treatment to exports from developing countries, such arrangement failed to serve as an effective mechanism of trade-creation and trade diversion in favor of developing countries.*50 Most economists agree that MFN tariff reduction is a more effective mechanism than the Generalized Preference System in improving market access of developing countries.*51 A new device was adopted in the Agreement on Differential and More Favorable Treatment, Reciprocity, and Fuller Participation of Developing countries*52 concluded during the Tokyo Round. The agreement provides a permanent legal basis within the GATT for preferential treatment to developing countries. Tariff reductions negotiated under this agreement is different from the GSP in that the benefits of the tariff concessions agreed on shall be automatically extended to all GATT member countries, and the MFN rule is therefore not eroded. The differential and more favorable treatments provided are the waivers of reciprocity by developed countries in negotiating tariff cuts. Priority was given to negotiations of tropical products, which are of special interest to developing countries, and substantial cuts have been achieved.

In so far as non-tariff trade barriers are concerned, it was estimated that four major types of non-tariff barriers, i.e. quotas, levies, licensing and export restraints, cover approximately one-third of the trade with developing countries.*53 Non-tariff trade barriers are generally concentrated on those industrial and agricultural sectors which are considered politically or economically sensitive in that they involve high inputs of low skilled labour.*54 Both the International Antidumping Code and the MTN Subsidy/ Countervailing

Duty Code provide special rules for developing countries. However, the Tokyo Round failed to solve the safeguard issue which is most crucial to the interest of developing countries. Many import restrictions against developing countries were imposed under the safeguard clause of national trade legislation. Moreover, voluntary export restraints negotiated with developing countries are even beyond the control of the GATT. In the Tokyo Round, efforts have been made to produce a safeguard code to impose stricter disciplines on the use of safeguard measures and to include VERs into the scope of the safeguard code. Negotiators were unable to compromise their differences over the problems of selectivity, and compensation for damage caused by safeguard action. Both Japan and developing countries strognly opposed the proposal that safeguard action can be taken selectively, i.e. an importing country is allowed to act against some of the exporters of a specific product without regard to the MFN principle. To allow selectivity will give importing countries a freer hand to take safeguard action.

Textile Trade

The multilateral arrangements in textile trade are the first effort made between developed and developing countries to meet structural changes in the textile sector. In the late 1950s and the early 1960s, the textile industry in developed countries bagan to decline when facing with low-cost competition from devloping countries. The existing bilateral trade agreements at that time were unable to cope with the rapidly increasing number of competitors from developing countries. A multilateral arrangement to establish an orderly trading conditions could not only protect the interests of developing countries but also ensure a smooth process of adjustment to the changing structure of relative costs in textile manufacture. The first of this kind of market arrangement is the Long-term Cotton Textile Agreement of 1962.*55 The Agreement requires importing countries with quantitative restrictions to undertake progressively to enlarge them. And where no quantitative restrictions applies, the agreement allows importing countries to introduce them if their markets are disrupted, but the restriction should be progressively relaxed. The imposition of new quota is subject to carefully designed rules regarding the initial levels and the formula for progressive expansion. However, these rules could be escaped by voluntary bilateral agreements. The Agreement however proved unsuccessful in effecting adjustment in developing countries. In spite of the dissatisfaction from exporters about the 1962 Agreement, a new agreement,i.e. the Arrangement Regarding International Trade in Textiles (also known as the Multi-fiber Arrangement, MFA) was reached in December 1973.*56 The MFA covers a wider range of textiles but its structure is essentially the same as the 1962 agreement.

Before the conclusion of the MFA, the U.S. had entered into comprehensive restrictive agreements with all its leading suppliers. In addition, the competitiveness of its textile industry seemed to have improved sharply after 1973. Under such circumstances, the U.S. was prepared not only to liberalize the terms of its bilateral agreements to bring its leading suppliers into the scope of the MFA, but also to grant large quota increases to other suppliers to exchange for bringing them under restriction. In contrast, the EEC was suffering from the decline of the textile and clothing industries.

Because of the inability to anticipate the slowdown of the Community's economy and the trade diversion effects of the more protective policies pursued by the U.S., and to coordinate the policies of the member countries sufficiently rapidly, the EEC took a rather relaxed attitude in controlling imports.*57 The restrictions applied were less comprehensive and a number of Mediteranean countries remained completely unrestricted and benefited from tariff preference. Small developed countries were unable to make developing countries to negotiate bilateral agreements, and therefore they had relatively frequent recourse to safeguard action under the market disruption clause of the MFA. Canada and Australia even bypassed the MFA, and took safeguard action under Article XIX of the General Agreement, regardless of the objection from the Textile Surveillance Body, and greatly eroded the standing of the MFA and its surveillance machinery.

Under the pressure from the EEC, the MFA was renewed in 1977 on the basis of a revised version of a protocol drafted by the U.S. The MFA II contains a crucial clause which allows "jointly agreed reasonable departure".*58 Thus, the U.S. was able to set initial quotas and subsequent growth rates well below those stipulated in the MFA. The EEC succeeded, before the MFA II was open to signiture, in negotiating bilateral agreements with its main suppliers to cut back quota drastically by threatening to initiate safeguard action under Article XIX of the General Agreement. The EEC also created a comprehensive quota system which has changed the MFA fundamentally under the "reasonable departure" clause. Small importing countries delayed rejoining the MFA until they could obtain restrictive agreements with their principal suppliers. These newly negotiated bilateral agreements were highly restrictive, cutting back quota up even to 15 per cent. Low annual growth rates were justified by the use of the "Scandinavian clause"*59 allowing "low positive rates" in countries with small markets to protect "minimum viable production". Australia is staying out of the MFA applying its own quota system under Article XIX of the General Agreement. Keesing and Wolf commented on the actual application of the MFA as follows:

> " What has since been in effect has been a departure from a departure --- a waiving of the provision of an agreement which itself was a derogation from GATT principles."*60

Developing countries tried to retaliate. Indonisia hit back by transferring contracts which might otherwise have gone to British companies to other contractors, when the U.K. persuaded the EEC to turn down an Indonisia's request for an increased textile quota under the MFA.*61

As the MFA was to expire by the end of 1981, negotiations were open in Geneva in July for its renewal. Developing contries put forwards a list of proposals to prevent the EEC and the U.S. from introducing more import curbs in a renewed MFA. They demanded that (1) there should be no distinction between imports from low-cost countries and those from other suppliers; (2) if protection was needed, imports should first be cut back from the largest supplier countries, e.g. the U.S. in the EEC markets; (3) there should be no discrimination between wealthier and poorer ones; (4) there should be clear-cut and objective criteria to define "market disruption"; (5) the MFA renewal should be accompanied by a "definite, detailed and time-bound programme for the implementation of adjustment measures"; and (6) the TSB should monitor import curbs. The EEC, on the other hand, took the position that imports into the EEC had to be curbed and their growth rates to be kept to within 15% of yearly growth in

Community demand for textile and clothing. Moreover, the Community needed a five-year period to allow its domestic producers to adjust to competition from developing countries. Thirdly, the EEC demanded to be allowed to curb any developing country's imports without prior consultation if the imports disrupted its domestic markets. After a long period of intensive negotiations, a protocol of extension was produced which reaffirms some of the rules embodied in the MFA and contains no important changes.

CONCLUSION --- Sectoral Approach to Trade Conflicts

The above sector-by-sector discussions of trade conflicts have shown how trading nations distorted legal mechanisms and evaded legal constraints in practicing protectionism with regard to those sensitive sectors. The only successful instance where trading nations solved their conflicts through multilateral negotiations is the harmonization of national export credit policies. The resolution reached did not follow the market force as factors of competition in this sector have been complicated by various government general as well as specific policies and the determinants of comparative adavantge became obscure. The resolution is rather a compromise which reflects the margin of competitive advantage that a country are allowed by other countries to maintain. In contrast, when the sector is defined in terms of product, comparative advantage is not allowed to be the sole determinant in market arrangement, because the production of the product involved is of vital importance to the social balance of importing or exporting countries. In the absence of international arrangements specifically directed at these sensitive sectors, countries therefore resorted to protective means which greatly distorted the existing trade rules, or to means that can evade the constraints imposed by trade rules. A sectoral arrangement may have the effect of insulating a sensitive sector from those sectors where trade patterns are not so much affected by the cyclical or structural changes. This could prevent the spreading of distortion in the application of trade law to non-sensitive sectors. Moreover, under a sectoral framework an arrangement can be made so that both exporting and importing countries could share the inevitable cost of changes in world economy on an equitable basis, and distortive application of law can be minimized. The main impediment to this sectoral approach is the definition of each sector. This is because of the input-output linkages between industries in a modern economy. Negotiations in a narrowly defined sector would inevitably affect the relative cost positions of the user industries or even those of its input industries. As to the general pattern of this kind of sectoral arrangement, the MFA provides a sound model, saving those sofening clauses which have the effects of frustrating the original purpose of establishing a sectoral framework. The sectoral approach to sensitive industries is the main foundation of the legal reform in international trade as proposed in this thesis. In the concluding part of this thesis, more on the sectoral approach can be seen.

Footnotes (Part one, Chapter III)

1. R.W. Rosendalh, "Border Tax Adjustments: Problems and Proposals", 2 Law and Policy in Int'l Buss. (1972) pp.85, 88
2. H. Johnson & M. Krauss, "Border Taxes, Border Tax Adjustments, Comparative Advantages, and the Balance of Payments", Canadian J. of Economics (1970) pp.595, 596
3. The rules appeared in an illustrative list of export subsidy prepared by a GATT working party in 1960. This list was incorporated into the MTN Subsidy/Countervailing Duty Code of 1979. BISD 19S/185, 26S/80-3. In item (g) of the list, it is provided that the "exemption or remission in respect of the production and distribution of like products when sold for domestic consumption" is a practice of export subsidy.
4. Border Tax Adjustment , Report of the Working Party adopted on 2 Dec. 1970, L/3464, BISD 18S/97
5. Letter to U.S. Steel dated Oct.20, 1975; reproduced at p. 78 of the Joint Appendix submitted to the U.S. Supreme Court in Zenith Radio Corporation v. United States
6. Zenith Corporation v. United States, 430 F. Supp.242 (Cust.Ct. 1977); 562 f.2d 1209 (C.C.P.A. 1977); 437 U.S. 443 (June 21, 1978)
7. The Revenue Act of 1971, P.L. 92-178, amended by Sec.1101 of the Tax Reform Act of 1976 and Section 991-7 of the Internal Revenue Code. For material regarding the DISC legislation and actual practices, see W.C. Gifford & W.P. Streng, 'International Tax Planning', pp. 33-84
8. Joint Committee Staff, General Explanation of the Tax Reform Act of 1976. An excerpt of this document can be seen in W.C. Gifford & W.P. Streng, pp. 72-82, see note 7
9. GATT document L/4422, L/4423, L/4424, L/4425, BISD 22S/105
10. J. Pearce, 'Subsidized Export Credit', pp.v; see also Statement on Burne Union, prepared by U.S. Department of Commerce, reprinted in Hearing on the East-West Trade Before the Senate Committee on Foreign Relations, 88 Cong. 2nd Sess. 354 (1954).
11. Pearce, see note 10, pp. 47-9.
13. GATT Illustrative List of Export Subsidies, Item (j), Report of the Working Party BISD 9S/185
14. Agreemnent on Interpretation and Application of Article VI, XVI, XXIII, BISD 26S/56, 81
15. Pearce, see note 10, pp. 47-9
16. The minimum rates reached are as follows.

Duration of loans	2-5 years	5-8.5 years	8.5-10 years
Country category			
Relative rich	11.0 (8.5)	11.25 (8.75)	n.a.
Intermediate	10.5 (8.0)	11.0 (8.5)	n.a.
Relatively poor	10.0 (7.5)	10.0 (7.75)	10.0 (7.75)

present interest rates in parenthese
source: Financial Times 12 Oct. 1981

17. T.E. Joseling, 'Agriculture in the Tokyo Round Negotiations', p.9
18. For current U.S. agricultural policies, see J.R. Tarrant, 'Food Policies', pp.86-94; and EEC policies, pp.94-105; for agricultural policies of other developed countries, see B. Fernon, 'Issues in World Farm Trade', pp. 18-39; for U.K. agricultural policies, see T.E. Joseling, 'Agriculture and Britain's Trade Policy Dilemma'.

19. Trade in Agricultural Products , Report of the Committee on Consultation with the EEC, the U.S. and the U.K. (GATT)
20. Joseling, see note 17, pp. 4-6
21. Article 10 of the Subsidy/Counterviling Duty Code, BISD 26S/56
22. Agreement Regarding Bovine Meat, BISD 26S/84
23. Article III
24. Article IV
25. International Dairy Arrangement, BISD 26S/91; Annex II --- Protocol Regarding Milk Fat, BISD 26S/107
26. Article IV
27. Article V
28. R. Gilmore, "Wheat and Coarse Grains --- Stabilization or Status Quo" in 'A New International Commodity Regime' edited by G. Goodwin and J. Mayall, p. 77
29. The conflict in issue is that Australia and Brazil complained formally to the GATT about the Community's Practice of giving cash refunds to sugar producers to persuade them to export when world prices are below the Community's internal prices. The GATT investigating panels concluded that the refunds system amounted to subsidization under the GATT rules. They said that the system was a "permanent source of uncertainty in world sugar markets, and therefore constitutes a threat of serious prejudice" to Australian and Brazilian export interests. The panels' findings however were set aside by the Community on the ground that the damage done to those interests was not quantified. While the GATT was unable to either force the Community to change its internal policies or solve the dispute through multilteral consultations, Australia threatened to withdraw all its tariff concessions to the Community. The only concession made by the Community as a result was to withhold a part of its surplus and reduce its exports. This was not accepted by Australia which insisted that there should be limits on the Community's sugar production or on the size of the subsidy, or other fundamental changes in the Community's sugar system. As the confrontation went on, Australia further threatened to divert its government purchases from the EEC countries, while the EEC replied that it would impose restrictions on imports from Australia. This series of events presents an important test to the dispute settlement scheme upon which the GATT heavily relies in establishing an orderly trading system. The EEC also sought to reconcile its difference with other sugar producing countries within the framework of the International Sugar Council set up by the International Sugar Agreement.
30. K. Kawahito, "Japanese Steel in the American Market: Conflict and Causes", The World Economy, Vol.4, No.3, September 1981, pp.229
31. A.F. Lowenfeld, 'Public Controls on International Trade', pp. 145
32. R. Dale, 'Antidumping Law in A Liberal Trade Order', pp. 149-158
33. U.S. Tariff Commission Pub. No.214
34. The escape clause is provided in section 301 of the Trade Expansion Act of 1962. Under this clause, the U.S. president is to grant assistance to an industry when "as a result in major part of concessions granted under trade agreements, an article is being imported into the United States in such increased quantities as to cause, or threaten to cause, serious injury to the domestic industry producing an article which is like or directly competitive with the imported article". The counterpart of this escape clause in the General Agreement is Article XIX. The national security clause appears in section 232(b) of the Act. Under this clause the president

is to take such action he deems necessary to adjust imports of an article or its derivatives, when the imports of such goods threaten to impair the national security of the U.S. The counterpart of this clause in the General Agreement is Article XXI. The "orderly marketing" provision is stipulated in section 352 of the Act. Under this provision, as an alternative to adjustment assistance and tariff adjustment, the president when conditions set in section 301(b) are fulfilled may "negotiate international agreements with foreign countries limiting the export from such countries".

35. Consumer Union of the U.S. v. Kissinger , 421 U.S. 1004 (1975)

36. A Comprehensive Program for the Steel Industry , Report to the President by the Interagency Task Force, A. Solomon, chairman; Implemetation of Trigger Price Mechanism by the U.S. Treasury (Jan.9, 1978)

37. The resposibility was shifted to the Department of Commerce under a presidential order issued in January 1980.

38. Treaty Establishing the European Coal and Steel Community, Paris, April 18, 1951, miscelaneous series of treaties published by the H.M.S.O., No.4, Command paper 4863

39. Treaty Establishing A Single Council and A Single Commission of the European Communities, Brussel, April 8, 1965, Misc. No.7 (1972) Command paper 4866

40. Six General Report on the Activities of the Community Vol. II, p .50

41. Article 60

42. Dale, see note 32, p. 152

43. Commission Statement Concerning Basic Prices of Certain Iron and Steel Products, O.J. Dec. 1977, No. L/353/1

44. "Steel---If We Trust", Economist, Nov.8-14, 1980

45. "Chemical Reaction---Don't Fall into the Steel Trap", Economist, Nov.15-21, 1980

46. The functions of the International Trade Commission, formerly the Tariff Commission, are provided in the U.S. antidumping, countervailing duty, escape clause and other trade legislations. One of its main function is to determine whether an import has caused the required degree of injury to the U.S. industry in order to assist the administration to take appropriate action.

47. 506 F.2d 136 (1974), cert, denied 421 U.S. 1004 (1975)

48. The antitrust account was dropped in the appeal. Judge Mcgowan of the Court of Appeal stated that the district court's declaration "are not couched in adjudicatory form" and are "without judicial force of effect" and the Sherman Act issue disappeared from the case when the plaintiff stipulated dismissal of the antitrust account. However, he admitted that the resolution of the antitrust issue "would almost certainly have required the exploration by adversarial trial of a number of complex questions of fact of law, and the making of legal ruling in an area not distinguished for its simplicity."

49. France unilaterally bars Japan from taking more than three per cent of the market. Italy has an almost ban on Japanese imports. The U.K. has an industry-by-industry agreement holding Japanese cars back to ten per cent of the market.

50. S. Colt, 'Developing Countries in the GATT System', pp.77; A.J. Yeats, 'Trade Barriers Facing Developing Countries', p.151

51. G. Patterson, "Would Tariff Preference Help Economic Development?", Lloyds Bank Review, April 1956; R. E. Baldwin and T. Murray, "MTN Traiff Reductions and Developing Country Trade Benefits

under the GSP", E.J. March 1971; S. Colt, see note 50, p. 17
52. BISD 26S/203
53. Yeats, see note 50, p.123
54. Ibid
55. For history of regulating trade in textiles, see D.B. Keesing and M. Wolf, 'Textile Quotas against Developing Countries'; U.S. International Trade Commission, 'The History and Current Status of the Multifiber Arrangement', and 'The Multifiber Arrangement, 1973-1980'
56. Protocol Extending the Arrangement Regarding International Trade in Textiles, BISD 24S/5 (1973)
57. Keesing & Wolf, see note 55, p.58
58. Article 5.3, Conclusions of the Textiles Committee Adopted on December 14 1977 BISD 24S/28
59. Article 6, see note 58
60. Keesing & Wolf, see note 55, p.70
61. "Indonesia Fights", South, Vol. 3, December 1980, p.51

PART TWO

LAW OF SUBSIDIES, DUMPING AND SAFEGUARDS

Chapter I

Economics of Subsidies

Chapter I(A): Economics of Subsidies

(A) Definition of Subsidy

The term subsidy, in the broadest sense, can be defined as any government action which affects the relative position of production or consumption of a product to that of others. Thus, a lower tax rate or regulatory burden, or discriminatory public procurement policies in favour of certain line of product would constitute a subsidy. A narrower definition would only include government actions granting benefits through revenue or expenditure measures. This narrower definition is consistent with the GATT approach which limits the concerns of the provisions governing the use of subsidy to those subsidies involving fiscal contribution from governments. Other measures though having beneficial effects on a certain line of product are to be dealt with in those provisions concerning non-discriminatory treatment, government procurement policies, imposition of quota, standards and etc.. The third and the narrowest approach considers a subsidy as a negative tax in order to distinguish it from an ordinary tax. The second approach is followed throughout this thesis so as to conform with the legal framework of the GATT, except in those instances where the term "subsidy" is used in contrast to the term "tax".

(B) General and Selective Subsidies

General subsidies are subsidies granted on all products and services or on such a widespread basis that the effects on any specific product cannot be traced. General subsidies can be in the form of subsidies or tax reliefs to the employment of factors of production. Since general subsidies affect all industries more or less equally, their effects are similar to those of depreciation of a currency and would not seriously distort allocation of resources under a flexible exchange rate regime.

Selective subsidies are those granted on a selective basis, either to a firm or an industry, and would cause relative shift in trade and production.

(C) Corrective and Distortive Subsidies

As discussed in Chapter II of Part One, government intervention is justified in correcting domestic market distortions, and non-tariff measures are almost invariably preferable than tariffs in such a pursuit.*1 Corrective subsidies like distortive subsidies may have effects on trade flows, but they direct trade flows towards optimal levels rather than distort the existing optimal situation. The proposition that the use of non-tariff measures are more appropriate than tariffs in correcting domestic market distortions is based on the general theory that distortions should be tackled as closely as possible to their sources. *2 Pareto optimality requires that the imposition of tax or the use of a subsidy intended to correct distortions in consumption, production, or factor supply be on a non-discriminatory basis, i.e. there should be no discrimination between international and domestic trade.*3 For instance, a tax on imports or a subsidy on exports of goods subject to external economies or monopolistic pricing in domestic production, designed to remove the distortions, makes the relative marginal costs of these goods to consumers higher than the marginal costs to the economy. Thus, trade intervention in such a case would remove one distortion but create another one, i.e. consumption loss in the present case, and cannot lead to a situation of Pareto optimality. Moreover, a tax on imports intended to correct an external diseconomy of consumption would permit the marginal rate of transformation of domestic resources into importable goods concerned to exceed the marginal rate of transformation through foreign trade. This is again a violation of

Pareto optimality because of the resulting production loss. Nonetheless, a departure from the rule of non-discrimination could still improve the level of welfare attainable under free trade in some cases.*4 This is because in some cases although a marginal departure from free trade conditions will result in a marginal consumption or production loss, it will also produce a non-negligible welfare gain if it moves the economy from a distorted position towards a Pareto-optimal equilibrium position. This proposition is however subject to the constraint posed by the theory of second best according to which it is impossible to predict whether the substitution of one distortion for another will in fact worsen or improve economic welfare.*5

Trade intervention is appropriate to correct distortions in the trade sector. For instance, when a domestic firm overestimates the risks of overseas operations and underestimates the effectiveness of its own government's assistance when faced with foreign restrictions, there thus exists an external economy and the government is justified in granting export subsidies, such as export quarantee.*6 Moreover, government intervention in the trade sector can also be allowed when the knowledge a firm acquired in opening up a new foreign market is transferred to its domestic competitors without costs. When there are distortions in foreign markets owing to imperfectly elastic foreign demand or supply, the imposition of optimum tariff, under the condition that there is no possible retaliation, could maximize the national welfare of the tariff-imposing country.*7

(D) Export Subsidies

Export subsidies ~~are~~ usually refer~~red~~ to subsidies granted solely to exported goods. Export subsidies are generally considered more condemnable than other kinds of subsidies, because (1) with a few exceptions, they are aimed at the increase in exports of a particular line of products and their effects on trade flows are more direct and in most cases more damaging to the trade interests of other countries; (2) they are less of an efficient instrument in correcting market distortions, most of which exist in domestic markets; and (3) they are also less useful in achieving non-efficiency objectives, such as redistribution of income among regions or sectors, because of the resulting consumption loss which can be avoided if production or income subsidies are used.*8 There are however two exceptions. First, when there exist distortions in the trade sector, corrective export subsidies are not distortion-creating but distortion-removing. Nevertheless, instances of this kind are rare. Secondly, when export subsidies are accompanied by import tariffs at the same rate, the effect of such a scheme is similar to that of depreciation of a currency at the same rate. There are no distortive effects on trade flows as a result.*9

In the following, various kinds of export subsidies will be discussed.

(1) Currency Manipulation

Devaluation of a country's currency can have the effect of reducing the prices of exports and under certain condition can successfully improve a country's balance-of-payments position.*10 Devaluation is also a preferred adjustment mechanism than tariff or non-ariff measures, because it does not cause distorting effects if policies for maintaining internal and external balances are effective and resources are allocated efficiently.*11 However, the experience of competitive devaluation in the inter-war slump teaches that there shall be limits on the use of devaluation. The change from a fixed to a managed floating exchange rate system and the weakening of the IMF's disciplinary power do not mean that countries may devaluate more freely in serving their commercial policies. Changes in exchange rates are still under international surveillance, though not within the framework of the IMF, and the inflationary effects of devaluation have further deterred governments from employing such an instrument.

Devaluation often proves to be politically infeasible in correcting deficits as it may hurt a country's international prestige. A system of uniform export-subsidy/ import-levy on all commodities and services, which has the same effect as devaluation in the current account, has been argued by many as an alternative solution. It may ease deficit pressure before deflation methods of adjustment, such as controls on wage increases and improvement in productivity, take effect.*12 The substitution of a scheme of uniform export subsidy/import levy for devaluation is not without difficulty. First, the scheme will not practically be administered so carefully as to apply to all commodities and services equally, and thus will result in a multiple exchange rate system.*13 Second, the scheme does not apply to the trasfer of capital and thus will result in a dual exchange rate system, even if the government can avoid the first difficulty.*14 Third, like devaluation, there shall be limits on the level of subsidies and levies in order to prevent abuse or misuse.

A multiple exchange rate system is the most blantant type of currency manipulation intended to boost exports. Under the system, more advantageous exchange rates are granted to exporters in converting their foreign earnings into national currencies or in purchasing foreign exchanges for importing materials for the production of exported goods. A regime of export-subsidy/ import-levy at various rates may have the same effect on trade flows as that of a multiple exchange rate system.

Multiple exchange rate practices are prohibited under the IMF Agreement, but exceptions are allowed for those Article 14 countries, i.e. countries in a transitional period such as developing countries. The reasons for allowing exceptions for developing countries are that they need foreign exchanges to finance their economic development and that a system of multiple exchange rate can help to remedy the failure of price system in allocating scarce foreign exchange and the inability to redistribute income through domestic means.*15

(2) Border Tax Adjustments

Export subsidies can also arise from excessive refunds or unjustified exemptions of internal taxes to exported goods. The principles of destination and of origin form the basis of economic as well as legal rules in this regard. An understanding of the reasons for the adoption of either of these two principles when different types of tax are concerned is essential for the analysis of GATT rules on border tax adjustments.

(a) Classic Tax-Shifting Assumption and Trade Neutrality of Tax Policies

Classic tax theories assume that indirect taxes are fully shifted forwards to consumers and thus fully reflected in sales prices, while direct taxes are fully shifted backwards to producers and therefore do not affect prices. Hence, tax adjustments are needed for indirect taxes in order to preserve tax neutrality. Under this assumption, exemptions from or rebate of direct taxes to exported goods, and refunds of internal indirect taxes which exceed the rates applied to domestically consumed goods would constitute export subsidies. However, there have been growing doubts on the soundness of this assumption. While economists generally agree that indirect taxes are shifted forwards and direct taxes backwards, they could not agree on the level of shifting, most of them accept that taxes are not fully shifted. The degree of shifting is, in effect, determined by various factors, including the elasticity of demand for the product concerned, the stage of business cycle, actions of monetary authorities in controlling money supply, the degree of competition among producers, the level of employment, flexibility of wage rates, and governments' fiscal policies.*16

Even assuming indirect taxes are shifted forwards and direct taxes backwards fully, trade neutrality may not be preserved in all cases after border tax adjustments. Trade neutrality can be achieved by the application of destination principle only when tax policies are similar among trading nations. When trade occurs between two countries, one placing emphasis on direct taxes and the other on indirect taxes as the source of revenue, producers in the former country would be at a disadvantageous position in competing with those in the latter country.

In addition to the consideration of trade neutrality, there are other considerations in dealing with border tax adjustment such as balance of payments effects, employment, tax sovereignty, and the allocation problem. These considerations will be discussed in the following in proper contexts.

(b) General Indirect Taxes

General indirect taxes such as value added taxes and turnover taxes cover all goods and services and are levied as a uniform percentage tax on them.*17 Changes in general indirect taxes that may have beneficial effects on a country's trade position can be in the following forms: (1) changes of general indirect tax system, (2) increases in tax rates, and (3) changes from direct to indirect general taxes. Ther first can be exemplified by the changeover from the turnover to the VAT system by EEC member countries. Since under the turnover system, it was impossible to calculate accurately the tax burden of each good and usually the calculation tended to be conservative, the change to the VAT system under which accurate calculation is possible would allow an increase in border adjustments, were the classic theory followed. Such an increase in border tax adjustment was regarded by the U.S. as a subsidy practice, while the EEC insisted that it be a corrective measure for the undercompensation under the turnover system. The second and the third kinds of changes can also result in increases in border adjustments under the destination principle. Thus, the resulting increases in border adjustment coupled with corresponding increses in import taxes make these three changes in effect indistinguishable from an uniform export-subsidy/ import-levy scheme, and an equivalent to a devaluation on trade account by the same percentage. However, under the origin principle, they would amount to an appreciation of a currency. It follows that under both principles, world trade and production would not be distorted.

Apart from the consideration of efficiency, one important issue with regard to general indirect taxes is their balance-of-payments effects. Under a fixed exchange rate system, increases in border adjustment without tax changes, e.g. the change from the turnover to the VAT system under the destination principle, would bring about a surplus in a country's balance of payments, but other countries would be faced deficit pressures and their unfavorable effects on real income and employment. This would allow unnecessary devaluation by a country already in a balance-of-payments surplus position.

In the case that a country increases its level of general direct taxes and there is an accompanying increase in border adjustments (destination principle), the balance-of-payments effects can vary considerably depending on such factors as the nature of expenditure and monetary policies accompanying the tax rise, the relative marginal spending propensities of the government and private sectors, and the elasticities of aggregate demand and supply.*18 However, the use of the destination principle always has a stronger surplus-creating tendency than the use of the origin principle.*19

When a country shifts from a general direct tax to a general indirect tax system and profits taxes are treated as a cost element, under the destination principle which allows increases in border adjustments under such circumstances, the balance-of-payments effect will be similar to that of an increase in border adjustment without a tax increase, i.e. a surplus will develop.*20 If, according to the classic theory, changes in direct taxes are not considered having price effects, the shift from a general direct tax to a general indirect tax will increase production costs and prices will rise accordingly. The balance-of-payments effects under such circumstances would depend on the marginal spending propensities of profit receivers compared with other income recipients,*21 the nature of expenditure and monetary policies accompanying the shift,and the elasticities of aggregate demand and supply.*22 It is usually the case that a surplus is more likely to develop under the destination principle.*23

The above mentioned balance-of-payments effects will not be so serious under a completely flexible exchange rate system, because the effects can be offset by changes in the level of wage rates, provided wage rates are flexible. Thus, under a flexible exchange rate system or when wage rates are flexible, it makes no difference as to which principle should apply in so far as balance of payments is concerned. However, under a fixed exchange rate system, in determining which principle should apply to changes in general indirect taxes, one has to take into account the prevailing balance-of-payments positions, as well as concomitant changes in policies with respect to direct taxes, government expenditures, the size of money supply, and etc..*25

(c) Selective Indirect Taxes

Unlike general indirect taxes which cover all goods and services and are levied at an uniform rate, selective indirect taxes cover fewer items and the rates may vary among them. Changes in the levels of selective indirect taxes also affect balance of payments as well as trade and production.*26 The resulting disequilibrium in balance of payments can be eliminated by changes in wages and exchange rates. As to the effect on trade and production, the use of destination principle would result in distortion in the structure of world consumption because domestic consumers pay more than international consumers for the taxed product.*27 Moreover, under the origin principle, the marginal cost in the taxed industry falls below the international price and the structure of world production would thus be distorted.*29 Thus, it does not matter which principle should apply as both priciples cause distortion.

Apart from the efficiency consideration, there are two secondary considerations in deciding which principle should apply in the case of selective indirect taxes. The first is the relative seriousness of damage to domestic producers and consumers. If the origin principle is followed, foreign imports will be relatively cheaper than those domestically produced goods. Domestic producers will thus lose their market shares and exporters of the taxing country will be less competitive in world markets. Conversely, if the destination principle is followed, foreign imports will be subject to the levy of increased taxes and share the decreased demand with domestic producers, while exporters are compensated by border tax adjustments. Domestic consumers will be faced with higher prices. Damage to domestic producers and the resulting unemployment are generally assumed more serious than damage to domestic consumers.*30 Another approach to the analysis of the relative seriousness of damage is based on the nature of selective indirect taxes as taxes usually imposed on products with inelastic demand like tobaco. The adoption of the destination principle does not cause serious harm to consumers because consumption will not drastically decrease in response to the rise in prices.*31

Another secondary consideration is the notion of tax sovereignty according to which selective indirect taxes are usually used as an instrument of social policies. It will be necessary to levy such taxes on imports as well as on domestic goods, if such policies are not to be frustrated by consumers' preference over imported goods.*32

(d) General Direct Taxes

Since direct taxes are levied on all kinds of income and therefore affect all commodities, they should be regarded as general taxes and can be analyzed in the same way as general indirect taxes.*33 The application of the destination principle in the case of general direct taxes will confront with the difficulty of determining the rates for adjustments. If one tries to fix a rate for adjustment on a product in the case of profit tax, he will be faced with variations in (1) profit rates among industries, (2) profit rates among firms within an industry, and (3) profit rates of a firm overtime.*34 It may well be that profit percentages are different for any two products. If an averaging principle is followed in allocation, the result of adjustments will be a system of multiple exchange rates and consequently inefficiency in the allocation of resources.*35

(e) Taxes Occultes

Taxes occultes are taxes levied on goods or services used in the production process. They may be taxes on overhead items such as plant, energy, transportation, as well as taxes on goods physically incorporated as a part of the final product. To the extent that taxes are levied on goods that are used as intermediate inputs and have a common cost-raising element in all traded goods, the effects of taxes occultes are similar to those of general indirect taxes.*36 On the other hand, to the extent that the tax element varies among commodities, the effects are similar to those of selective indirect taxes.*37 Thus, the effects of taxes occultes are a hybrid of those of general and selective indirect taxes. The application of the destination principle under such circumstances would also be faced with the allocation problem. It is never easy to calculate accurately the element of tax on overhead items in the final product. Only when the tax is levied under the VAT system where the unique accounting design makes it possible to calculate the tax in a multi-stage production process, or the intermediate good is physically incorporated in the final product, the allocation problem poses no particular difficulty. If border tax adjustments are allowed only for taxes occultes levied under the VAT system or levied on intermediate goods physically incorporated in the final products, countries following a non-VAT system,e.g. the cascade system, and countries imposing relatively higher levels of indirect taxes on fuel or power will be punished by their own tax policies.

(f) <u>Drawbacks of Import Changes</u>

Tariffs, duties and other fiscal charges levied on imports are equivolent to selective indirect taxes and border adjustments for these charges would also be met with the allocation problem. If border adjustments are allowed for imported inputs physically incorporated into the final products only, there will be serious disadvantages to developing countries because of their greater dependence on imported machinery and technology.*38 Moreover, drawbacks for imported goods without similar treatment accorded to domestically produced goods would discourage domestic producers from using the latter in their production of exported goods.

(g) Earmarked Taxes

Earmarked taxes are selective indirect taxes whose receipts are earmarked to a specific government activity furnishing services to the taxpayers and therefore reducing input costs.*39 For instance, a government may finance its highway program by excise taxes on fuel, tires, and cars. Since the taxes are earmarked to a specific use and the rate of tax on an item is approximately equal to its share of costs of the activity, to allow border adjustments for such a tax would amount to an export subsidy. Under the VAT system, it is easier to single out the element of such a tax and there is no serious allocation problem in excluding it from border adjustments. Even under the cascade system, the allocation problem would not pose particular difficulties as earmarked taxes are principally levied on such input items as motor vehicles, machinery, office supplies, transportation and energy products, which are usually not incorporated in final products.*40

(3) Export Credit and Export Guarantee

Generally, official export credit or export guarantee programs operated by governments at terms more favorable than commercial terms for similar domestic transportations would divert resources from their most productive use.*41 Moreover, government lending of foreign currencies at terms more favorable than those available in international capital markets would also affect international trade. Whether a government incurs losses in such pursuits is not particularly relevant in so far as world efficiency is concerned. It may be that for some transactions there are no commercial terms available because the risks involved have not been estimated by actuarial computation.*42 It is also possible that there exist externalities because the risks involved are habitually overestimated by the commercial sector. Under such circumstances, it is impossible or inappropriate to apply commercial terms in the assessment of subsidy elements in government sponsored export credit or guarantee. Inter-governmental consultations are particularly important in establishing a common criterion.

To apply commercial terms in disciplining well established subsidy practices in export credit and export guarantees will hardly be acceptable to practicing countries. Moreover, since the effects of subsidies offset one another, it is difficult to decide on what basis a corrective or a countermeasure should apply. The use of commercial terms as a basis will result in further distortions. The difficulty in applying commercial terms is also resulted from the divergence in interest rates among trading nations. In those countries adopting monetary approach in controlling inflation, domestic interest rates are usually maintained at high levels in order to limit money supply. Governments may feel obliged to grant assistance to exporters in credit arrangments so that exporters will not be victimized by domestic monetary policies. This is even more so, when a country's interest rate is not raised as a result of domestic policies, but those of other countries.*43 Meanwhile, in those countries like Japan, interest rates are maintained at low levels because of ration arrangements which distribute available resource and limit access to capital markets. Such low levels of interest rate may not be acceptable to countries with high interest rates as fair criteria in assessing export credit arrangements.

Among those methods that have been developed for the control of export credit arrangements, the Burne Union approach allows member countries to adopt the most liberal terms offered by any other members. This approach is unsound, because it tends to result in the so-called "customary term" applied by all countries even though interest rates vary substantially from country to country partly due to the relative abundance or scarcity of capital in different countries.*44 The GATT approach which uses the costs of financing in defining export subsidies in this regard is inadequate to remove distortion caused by the divergence from commercial terms. The present OECD approach which establishes uniform rates to be applied to all member countries is also inadequate unless interest rates among trading nations are approximately the same. The differentiated rate system (DRS) proposed in the Wallen Report, in which a different minimum interest based on market rates would be established for each currency, is sounder, because it links the minimum rate with prevailing market rates. Another method also proposed in the Wallen Report is the uniform moving matrix (UMM) which provides a single minimum interest rate for all currencies and the rate would move automatically according to changes in average market rates. This approach, though flexible, also fails to take into account the difference in market rates and to remove existing distortion.

Another important issue in export credit is mixed credit which offers more favourable terms for developing countries as a kind of foreign aid. Mixed credit is absolutely welcome as long as it is not tied to the purchase of commodities from the aid-giving country,i.e. all countries have an equal chance to bid for the purchase of the aid-receiving country. Whenever the aid is tied to purchases from an exclusive source, the pattern of world trade would be affected. However, it was argued by Professor Barcelo that mixed credit tied with sales to developing countries should be allowed, because a system of tied aid is better than no aid at all.*45 The validity of this argument is weakened by the fact that suppliers in the aid-giving country often take advantage of the tied aid and charge inflated prices to which the aid-giving country pays in the first instance and the aid receiving country pays in the end.*46 The best way to deal with the aid issue is to inject more capital into international financial institutions, such as the IMF, the World Bank, the International Finance Corporation, or regional development banks, and thus enable them to provide funds for developing countries at more liberal terms. There is however a valid argument for allowing subsidies in export financing when the financial markets are unable to supply credit at terms acceptable to the developing countries. *47 This often happens in investment in developing countries' infra-structure which entails operation exceeding in size and in time what private financial institutions can afford without governmental support.

(E) Subsidies Other Than Export Subsidies (Domestic Subsidies)

Export subsidies are discriminatory subsidies granted to exported goods only. Subsidies other than export subsidies include: (1) subsidies granted without discriminating whether the subsidized goods are to be exported, so long as they are domestically produced, (2) subsidies granted without discriminating whether the subsidized goods are domestically produced, so long as they are for domestic consumption, and (3) subsidies granted exclusively to goods which are domestically produced and for domestic consumption, e.g. consumption subsidies granted to domestically produced goods only. If subsidies are treated as negative taxes and analyzed in the same way, (2) will amount to the use of domestic subsidies under the destination principle and (1) is the use of domestic subsidies under the origin principle. The third is the opposite of export subsidies in so far as discriminatory subsidies are concerned.*48 Subsidies other than export subsidies are generally considered more acceptable or sometimes more desirable, because (1) such subsidies are more often used to correct market distortions, most of which exist in domestic markets, and (2) such subsidies often serve as an instrument in achieving national objectives and their trade effects under such circumstance are the secondary consideration of the practicing governments. However, the trade effects, though indirect, are not necessarily less distortive than those of export subsidies.

In the following, two forms of subsidies other than export subsidies, general and selective subsidies, and subsidies linked with various objectives will be examined. For the convenience of discussion, subsidies other than export subsidies are sometimes referred as domestic subsidies, although in a strict sense, they are not equivalent.

(1) General Subsidies Other Than Export Subsidies

Included in this category are public education, bridges, roads, and other benefits that are available to all sectors. Although such a subsidy benefits each sector unevenly, it still constitutes a common cost-reducing factor. Moreover, since general subsidies do not discriminate one line of production from the other, they usually do not distort the allocation of resources. But they would affect balance of payments. The effects on balance of payments can be offset by changes in exchange rates under a system of flexible exchange rate, or changes in wage rates when wages are flexible. When both exchange rates and wage rates are not flexible, whether the destination or the origin principle should apply will depend on the prevailing balance-of-payments position.

The provision of public goods through general subsidies is one of the major functions of a modern state, as the society is increasingly urbanized and specialized.*49 This is because of the nature of public goods, namely, the quantity available does not diminish with enjoyment or it is costly or inconvenient to charge for them pro rata consumption.*50 Moreover, the society may prefer public supply to private supply of certain private goods, such as education and health.*51 Thus, the nature of public goods and the social preference for public supply together with minimum trade effects lead to the conclusion that general subsidies other than export subsidies should not be a serious concern in international trade.

(2) Selective Subsidies Other Than Export Subsidies

The effects of selective subsidies on items that are not widely used as intermediate inputs are comparable to those of selective indirect taxes and can be analyzed in the same way.*52 Under the origin principle, subsidies are not extended to imported goods and exported goods do not return the susbsidies received. Hence, the competitiveness of foreign producers is affected in the same way (but not in degree) as by export subsidies or import duties. Although an inequity in marginal production costs among trading partners is caused as a result, an equity in consumer prices can be maintained.*53 Under the destination principle, however, there would be an inequity in consumer prices but an equity in marginal production costs can be maintained. Both principles result in distortions, but they cannot be ranked in terms of which principle reduces potential income more.*54 It is however impossible for a subsidizing country to adopt the destination principle, because the main purpose of granting subsidies, namely, resisting foreign import competition, would be frustrated by extending the subsidies to foreign imports. When subsidies are granted exclusively to goods which are domestically produced and consumed, there would be an inequity in marginal production costs as well as in consumer prices.

(a) Regional Aids

It is common for governments to grant subsidies to assist economic development of a specific region in an attempt to narrow down the difference in economic conditions between that region and others. Differences among regions can be attributed to market imperfection, especially the immobility of factors of production,*55 or geographical differences. When subsidies are aimed at the former differences, they are efficiency-improving; when aimed at the latter differences, they may be due to the social preference for balanced development among all regions of a country. With regard to the first aim, several points can be made. First, just as the infant industry argument for protection in the case of the less developed countries, the infant region argument can be made for the underdeveloped regions within a country's boundary. A case of infant region can be seen where a group of industries, having a degree of interdependence and external economies of location in the same area, will, after a short period of protection, be both nationally and internationally competitive in the long run.*56 Second, when there exist short-term obstacles to mobility, policies aimed at moving labour out of or capital into a region are appropriate.*57 Subsidies of this kind also include subsidies intended to promote intra-regional industrial or occupational mobility.*58 Although the efficiency-improving argument is theoretically sound, it is subject to the difficulty of predicting whether the subsidies granted will eventually improve efficiency at all, because of the difficulty involved in making a long-term cost/benefit analysis on the future prospects of a region.*59

When regional aids aimed at efficiency-improving objectives exceed what are needed in such pursuits, there will be distortions. Moreover, other than these objectives, regional aids are often used to maintain employment in a specific region or to achieve other objectives of social preference. It is inevitable that there will be distortion as a result.

Trade effects of regional aids which are available for all industries within a region may not be so significant as those of industry-wide subsidies. But trade effects may appear more sentitive in an economic union where internal tariff barriers have been removed. When regional aids are granted to a region endowed with one single industry, the effects of such subsidies are more significant than those of subsidies to a region with a more complex industrial structure. Similarly, when regional aids are directed to assist the establishment of a new industry not previously existed in the country concerned, the effects will concentrate on international trade.*60

(b) Subsidies As An Instrument of Industrial Policies

Traditional government roles in industrial development are the maintenance and the development of legal framework for business, the regulation of public utilities, and the use of tariffs for the protection of domestic industries. When trade restrictions are no longer easy to resort to and domestic industries are more and more exposed to international competition as a result of GATT negotiations on tariff reduction and growing integration among trading nations, new forms of industrial policies have thus emerged. Modern industrial policies can be classified into two categories: (1) positive industrial policies whose aims are to correct market distortions, or to assist adjustments to structural changes either by promoting new industries and high technology, or to help the restructuring of old industries; and (2) defensive or negative industrial policies directed to slow down or to assist resistance to structural changes, or even to keep alive declining industries. Positive industrial policies are consistent with global efficiency, while negative industrial policies can only be justified on non-efficiency grounds.

(i) Positive Industrial Policies: Research and Development

Justification for government support of R&D often rests on the externalities that can be generated and the risks that may involve. Public support can avoid underinvestment in this area. Special depreciation provisions for investment in R&D, and directly or indirectly subsidizing innovations are common forms of government supports. The difficulty in the application of the R&D justification lies in the determination of which lines of research are to be encouraged. Investment in research on basic science is an obvious case, becuse it can generate externalities most,*61 and is usually not covered by a patent system. Research in high technology which can accelerate the process of establishing new industries to utilize resources released from old industries is also worth supporting, and its commercial variability is the appropriate test for support.

(ii) Positive Industrial Policies: Adjustment Assistance

As discussed in Chapter II of Part One, factor mobility, especially labour mobility, in developed countries is unable to keep pace with the rapidity and scale of structural changes. Adjustment assistance is necessary to remove obstacles to factore mobility and to alleviate social problems accompanying such immobility. The need for government intervention arises not only from import competition or the loss of third country markets for exports, but also from domestic changes in response to improvement in productivity due to technology innovations. In all cases, the concern of adjustment assistance is to move resoures out of socially less useful activities to more productive pursuits. An adjustment assistance program would involve the provision of assistance to the contraction or even shut-down of an ailing firm, to the expansion of a firm engaging in a new adventure where resources can be most efficiently used, or to the restructuring of an existing firm which will become competitive again as a result. As far as import-related adjustment assistance is concerned, it apperas to be a compromising mechanism for the rival interests between domestic consumers and producers.*62 Moreover, a successful adjustment assistance program would reduce the need for safeguard actions. Even when a safeguard action has been taken, adjustment assistance can speed up the adaptation process of domestic market disrupted by imports, and therefore shorten the duration and minimize the damaging effects of the safeguard action. Most importantly, withdrawal from industries that developed countries no longer maintain comparative advantage can improve the market access of the developing countries. Adjustment assistance granted to domestic sectors from this standpoint functions as development assistance to developing countries.*63

(iii) Defensive Industrial Policies

When an adjustment assistance program is inadequate either in speed or in scale to meet structural changes, governments may grant subsidies to lighten the competitive pressure on a domestic industry or firm. This is especially true when the industry or the firm concerned is of great significance to the society or employs a great deal of labour. Subsidies of this kind tend to be permanent. Secondly, government may grant subsidies to a domestic industry simply because other governments are granting the same subsidies to their domestic industries. Thirdly, government assistance to a declining industry may be considered necessary because the industry is important to the government's defence strategy.

(F) Subsidies and Primary Commodities

In dealing with subsidies on primary products, there are two areas of interest: (1) domestic price stabilization and price support schemes, and (2) export subsidies linked with domestic price support schemes. As discussed in Chapter III of Part One, these practices are common and sometimes one of the major functions of national governments. Discussion in this section will concentrate on the analysis of the characteristics of markets for primary commodities and of trade in this sector. The main concern will be on agricultural products, because this is the main area where international disputes regarding subsidies on primary products arise from. Other primary commodities are generally the concerns of international commodity agreements aimed at stablization of prices at the international level. This does not mean that subsidies on agricultural products are irrelevant to international commodity agreements. In fact, several international commodity agreements, concluded either within or beyond the framework of the GATT, are directed to deal with subsidies on agricultural products or have some degree of influence on the subsidy practices.

In an efficient market, prices are themselves sufficient indicators for production and consumption decisions, since all variables in the market have contributed to the price formation.*64 Agricultural production has a number of characteristics which distinguish it from production in other sectors and prevent prices from performing as an efficient mechanism in the allocation of resources. First, agricultural production is the result of the activities of a large number of individual producers. This deters producers from reacting accurately to changes in the marketplace, because the interconnection between the producers and the markets can be adequately facilitated only when there are few actors on the supply side.*65 Second, the large number of producers, each of whom has a minimal amount for sale at one time, weakens the producers' position in negotiating contract terms.*66 Third, there are seasonal fluctuations due to storage difficulty.*67 Fourth, the inelasticity of demand and the short-term fixity of supply resulting from substantial time lags involved in alterating output levels mean that supply and demand are likely to generate rapid and substantial short-term price changes.*68 Fifth, in the long term, the innovation of technology will lead to more rapid growth in supply than in demand and when alternative employment opportunities are limited, variable costs, largely labour costs, can be reduced to low levels.*69 This means a secular decline in farmers' income. The above mentioned characteristics indicate that there exist uncertainties in the market, and prices tend to be unstable and sometimes fail to give fair returns to producers. Uncertainties and their associated risks in agricultural product trade are more difficult to reduce through the operation of future markets, because private risk aversion usually exceeds that of the society as a whole and private traders may under-invest in stocks and under-utilize markets.*70

The uncertainties in the markets therefore call for stabilization arrangements. There are two seperate but related issues to be dealt with: (1) price stabilization, and (2) income stabilization and income maintenance. Studies show that the overall gains from price stabilization are positive, but the distribution of benefits between producers and consumers will depend upon the source of instability or the structure of the demand and supply curves.*71 Since price stabilization may also have beneficial effects on sectors of the society other than producers, government assistance to producers in establishing a common fund as an instrument of buffer-stock financing can be justified. Price stabilization is also used to achieve income stabilization, but both are not positively related.*72 The aim of income stabilization and income maintenance can be more appropriately achieved through buffer funds and compensatory financing operated by government independently of price stabilization.*73 Governments may even fix by law the minimum prices for agricultural products at high levels. The success of an income maintenance measure is however conditional on the isolation of the domestic market from world markets. Various mechanisms such as tariffs, quntitative import restrictions, equalizing import levies or mixing regulations are used. Nevertheless, these measures if unaccompanied by production control, tend to result in over-production. In order to prevent those surpluses from disturbing domestic prices, export subsidies are used to reduce the surplus pressure.

To the extent that there are no government funds involved in the operation of a price stabilization scheme, there is no question of subsidy, even though the scheme may result in domestic prices being higher than export prices. Price stabilization arrangements under such circumstances should be deemed as normal market behaviours. Even there is a subsidy involved in the operation of a price stabilization scheme, the subsidy can be justified because of the external economies that can be generated by the scheme. The use of domestic subsidies in such pursuits can be justified, so long as it is accompanied by appropriate production control. Export subsidies are the least justifiable, because they may directly affect the trade interest of other countries and the domestic goals can well be achieved without their use.

Apart from governement intervention in the domestic markets, the existence of non-competitive and non-market behaviours makes competition in the world markets far from perfect. First, there exist inter-governmental arrangements between producing countries in an attempt to stabilize world markets, and/or to force or to hold up prices for certain commodities. This can be exemplified by international commodity agreements regarding coffee, sugar, wheat, cocoa, meat and dairy products. Second, for commodities like wheat, substantial stock variations are often accepted by producers in preference to short-term price changes and by consumers because of an associated gain such as supply security.*74 Arrangements between producing and consuming countries may be made through long-term contracts, through administered prices, and through customary and established buyer-seller relationships.*75 Third, there may be arrangements to supply to developing countries on a non-commercial basis as foreign aids. There may also be arrangements which guarantee market access for agricultural products from developing countries. Fourth, some agricultural sectors are under substantial government control or influence, and transactions may be politicized to some extent.

The existence of various non-competitive and non-market arrangements makes the scope for free competition limited. Moreover, with so many variables in the marketplace, it is difficult to evaluate the effect of a subsidy practice on international trade, especially in the establishment of a causal link between the subsidy practice and the subsequent changes in the markets. There is also the problem of defining the market by reference of which the effect of the subsidy is to be evaluated.

(G) Subsidies and Pollution Control

As discussed in Chapter II of Part One, environmental assimilative capacity has been gradually considered as a source of comparative advantage like other factors of production. National standards for pollution control is another factor to be considered in determining the competitiveness of producers. Differences in national standards may affect the costs of production and the relative competitive relation among suppliers. To neutralize the resulting trade effects is therefore deemed by governments as another issue to be tackled in the efforts to control pollution. This section will examine the subsidy problem in both pollution control and neutralization of its trade effects.

The "polluter pay" principle (PPP) which has been accepted by the member countries of the OECD as the guiding principle for pollution control is considered by economists as the most appropriate implementation framework. The PPP means

> " that the polluter should bear the expense of carrying...measures decided by public authorities to ensure that environment is in an acceptable state. In other words, the costs of these measures should be reflected in the cost of the goods and services which cause pollution in production and/or consumption. Such measures should not be accompanied by subsidies that would creat significant distortions in international trade and investment. " *76

The most important advantage of the PPP is that it can minimize international distortions arising from pollution control. Under the PPP, production would shift in favour of countries with relatively better assimilative capacity, and countries which are more tolerant to pollution. Meanwhile, pollution control can be more efficiently achieved, because the internalization of the costs would exert pressure on producers to search for new technologies in order to reduce the capital and operating costs.*77 Third, that producers and consumers share the pollution control costs according to the relevant elasticity of demand and supply under the PPP conforms with the criterion of equity.*78 The PPP-induced shifts in demand patterns in turn reduce the extent of the residual damages of pollution at the source which is unavoidable because of the impossibility of zero-discharge of pollution.*80

The PPP can be implemented through special pollution regulations or a pollution tax schemes. The regulatory method is accompanied by penalties on non-conformance. The tax method would impose a tax on pollutors set at a level so that the cost of increasing pollution, at the margin, is greater than the cost of internalizing it. The tax is in effect a combination of a compensation tax for the resulting diseconomies and a punitive tax to encourage producers to conform with the pollution control standard. The adjustment process under these two price mechanisms like those in response to other changes in the pattern of comparative advantage may be socially painful in part because of the resulting unemployment, or regional or sectoral imbalance.*81 Thus, government adjustment assistance in the form of subsidies other than export subsidies may be desirable. Such use of subsidy should be distinguished from the subsidy approach in promoting environmental quality. The subsidy approach is less appropriate than the price approach,i.e. the regulatory and the tax methods, because it provides no incentive to adopt the least costly means in eliminating pollution.*82 However, the subsidy approach is often favoured by governments for it entails less price effects.

Governments may also intervene in the trade sector in order to temper the trade effects of the price mechanisms. This can be done by levying import charges and granting rebates of internal pollution taxes or penalities or other forms of export subsidies. If internal pollution taxes and pollution control regulation and its accompanying penalties are treated as selective indirect taxes, the application of the origin principle is more appropriate in the case of production pollution. This is because the PPP requires producers to bear the costs of control on production pollution. Thus, rebates of internal pollution taxes or penalties should be considered as export subsidy practices, and, together with other forms of export subsidy, should be considered unjustified. The same rationale would lead to a different conclusion in the case of taxes on consumption polllution arising from the use of either pollution-prone end products, such as automobiles, or pollution-prone input products, such as high sulphur content industrial fuel oil. The PPP in this case would allow border adjustment, because the polluters are consumers abroad in so far as exported goods are concerned. Similarly, government regulations setting minimum pollution standard need not apply to exported goods, but foreign imports should be subject to the regulations.

CONCLUSION

In this chapter, we have examined various types of subsidies and their effects on trade and production patterns. Subsidies are not necessarily distortive and they can be a corrective means against distortion. Subsidies in many instances are governments' instruments in achieving macro-economic or social-political objectives. Thus, in regulating subsidies, one should not use trade-restricting effects as the sole criterion. Instead, the underlying circumstances, e.g. current balance-of-payments position, employment, domestic income distribution, and social goals, should be taken into account. In the following chapter, we shall investigate how international law is designed to reconcile the international need for trade neutrality of subsidies as a policy instrument and the domestic need for subsidies in pursuit of a national economic or social-political goal. There are of course subsidies directly aimed at affecting trade neutrality without any accompanying macro-economic or social-political objectives. There is also the problem of how the conflict between trade neutrality and global effeciency, i.e. when a subsidy has an effect on trade neutrality but is not contrary to, or has positive effects on, global efficiency, is to be resolved under international law.

Footnotes (Part Two, Chapter I)

1. see Part One, Chapter II supra
2. Bhagwati and Ramaswami, " Domestic Distortions, Tariffs, and Theory of Optimum Subsidy ", J.P.E. Feb. 1963, p.49
3. G.H. Johnson, " Optimal Trade Intervention in the Presence of Domestic Distortions ", in H.G. Johnson, ' Aspect of the Theory of Tariffs ', pp. 124-7
4. Ibid, pp.120
5. Ibid, pp.126
6. J.J. Barcelo, " Subsidies and Countervailing Duties--Analysis and A Proposal ", Law and Policy in International Business, Vol. 9:779 (1977) pp.802-5
7. Johnson, see note 3, pp.118-9
8. Barcelo, see note 6, pp.709-11
9. R.E. Baldwin, ' Nontariff Distortions of International Trade ', pp.19-22
10. The condition is that the sum of absolute values of import elasticity and export elasticity of a country is larger than one.
11. This is because depreciation has the effect of encouraging both export and import-competiting production in a uniform manner and therefore does not lead to artificial expansion of one sector, as either export subsidies or import levies by themselves do. Baldwin, see note 9, p.48
12. Baldwin, see note 9, p.20
13. G.Haberler, " Import Taxes and Export Subsidies: A Substitution for the Realigament of Exchange Rate? ", Kyklos, Vol 20, 1967, Fasc. 1, pp.17-23
14. Baldwin, see note 9, p. 20
15. Baecelo, see note 6, pp.806-7
16. U.S. Executive Branch GATT Study No.1: Tax Adjustment in International Trade: GATT Provision and EEC Practices.pp.7; R.W. Rosendalh, " Border Tax Adjustment: Problem and Proposals ", 2 Law and Policy in Int'l Bus. 85 (1972) pp.108-112
17. Baldwin, see note 9, p.89
18. Ibid, pp. 91-3
19. Ibid, pp.95-6
20. Ibid, pp.93-4
21. Ibid.
22. Ibid, pp.91-3
23. Ibid.
24. Ibid, pp.96-8
25. Ibid.
26. Ibid, pp.100-2
27. Ibid.
28. Ibid.
29. Ibid.
30. M.von Steiaecker, ' Domestic Taxation and Foreign Trade: The United States-European Border Tax Dispute ', pp. 70; Barcelo, see note 6, p.812
31. Baldwin, see note 9, pp.103-4
32. Steinaecker, see note 30, p.102
33. Baldwin, see note 9, pp.108-9
34. Ibid.
35. Barcelo, see note 6, p.810
36. Baldwin, see note 9, p.105
37. Ibid
38. V.J.Kelkar, " GATT, Export Subsides, and Developing Countries ", J. W.T.L., p.368
39. Baldwin, see note 9, pp.104-5

40. Barcelo, see note 6, p.816
41. Baldwin, see note 9, p.53
42. K.Dam,' The GATT--- Law and International Economic Organization ', p .139
43. For example, the U.S. Government's refusal to intervene in the Federal Reserve Bank monetary policies has been keeping the U.S. interest at high levels, and consequently prevented the lowering of the interest in the European markets.
44. Baldwin, see note 9, pp.53-4
45. Barcelo, see note 6, pp.805-8
46. Gerard and Victoria Curzon, 'Hidden Barriers to International Trade 7, pp.22-3
47. Ibid
48. Export subsidies are only granted to goods which are domecstically produced and for foreign consumption, whereas those included in the (3) category only garnted to goods which are domestically produced and for domestic consumption. If the authority of the Italian Machinery case is followed, the (3) kind of subsidies are not to be governed by the antisubsidy provisions of the GATT. see the text accompanying notes 97-9 of this chapter.
49. Victoria Curzon Price, ' Industrial Policies in the European Community ', p.37
50. Ibid
51. Ibid
52. Baldwin, see note 9, p.112; For discussions of various types of selective subsidies linked with policy objectives, see Baldwin, note 9, pp.11122; Victoria Curzon, ' Industrial Policies in the European Community '; S.J. Warnecke ed el, ' International Trade and Industrial Policies '; G.Denton, S.O'Cleireacain and S.Ash, ' Trade Effects of Public Subsidies to Private Enterprises '; W.M. Corden and G.Fels, ' Public Assistance to Industry: Protection and Subsidies in Britain and Germany '.
53. Ibid
54. Ibid
55. G.Denton and S. O'Cleireacain, ' Subsidy Isuues in International Commerce ', p. 23
56. Ibid, p.24
57. Ibid, p.25
58. Ibid.
59. Ibid, pp.26-7; For a detailed analysis in this regard and of the trade effect of a regional aid, see G.Denton, S. O'Cleireacain and S.Ash, " Regional Subsidies and International Trade ", in ' Trade Effects of Public Subsidies to Private Enterprice '.
60. G. Denton, S. O'Cleireacain, and S. Ash, see note 58, pp.107-8
61. Baldwin, see note 9, p.129
62. Denton, O'Cleireacain, and Ash, see note 58, p. 238
63. Ibid, p.252
64. S. Harris, M.Salmon and B.Smith, ' Analysis of Commodity Markets for Policy Purposes ', p.6
65. J.R. Tarrant, ' Food Policies ', p.48
66 Ibid
67. Ibid, p.55
68. Harris, Salmon, and Smith, see note 63, p.20
69. Ibid
70. Ibid, pp.11-4
71. S.Harris, M. Salmon, and Smith, see note 63, pp.40-1.
72. Ibid, p.39

73. Ibid
74. Ibid, p. 25, This is especially true in commodity markets where there are significant production lags.
75. Ibid
76. O.E.C.D. Enviro,ental Committee, " Guiding Principles Concerning the International Economic Aspects of Enviromental Policies ", OECD Document C (72) 128, para. 4
77. C. pearson & Takas, ' International Economic Implications of Envion-mental Control and Pollution Abatement Policy in An Interdependent World --- Compendium and Papers ', pp. 784
78. I. Walter, ' International Economics of Pollution ', pp. 96-7
79. Ibid, pp.97-8
80. Ibid, p. 98
81. For a detailed discussion on possible departure from the PPP, see I. Walter, pp. 99-112
82. C. Pearson & W. Takas, see note 76, p. 784

PART TWO

LAW OF SUBSIDIES, DUMPING AND SAFEGUARDS

Chapter II

Subsidies under the GATT

Chapter II : Subsidies under the GATT

Introduction to the GATT Legal System

The basic structure of the GATT legal system is built on the non-discrimination and the MFN clauses which reflect the GATT's objective of pursuing a non-discriminatory and multilateral legal order. Both clauses are intended to prevent any disturbance to the functioning of the law of comparative advantage in determining world production and trade pattern by discriminatory measures. However, as mentioned in the Introduction of this thesis, for a trade-barrier-ridden world to be liberalized, the priciple of non-discrimination does not necessarily lead to a more liberalized world than without its application. The foundation of the principle is rather rested on the notion of sovereign equality. On top of the basic structure, there are rules aimed at elimination of trade barriers. New quotas, tariffs and all other import/export restrictions are prohibited. Exceptions are allowed when a country is facing balance-of-payments difficulties, sudden market disruption, or subsidized or dumped imports, or is in transition, such as developing countries. The balance-of-payments clause used to be a main excuse for countries to impose restrictions on imports. After the change from the fixed to the managed floating exchange rate system, the clause has seldom been invoked. Rather, countries began to turn to the antisubsidy, antidumping and safeguard clauses for excuses, when domestic political pressures required protection against imports.

With regard to the pre-existing trade barriers, mainly tariffs, several rounds of negotiation on tariff reduction has been held. The original negotiation pattern is that every two countries would first negotiate between themselves tariff reductions regarding products of their respective export interest. The negotiation is guided by the principle of reciprocity, i.e. the economic advantages that each of these two countries gives and takes is to their satisfaction balanced. The rates of tariff reduction thus reached should then be applied to all other contracting parties of the GATT. From the Kennedy Round onwards, the pattern has been changed to across-the-board tariff reduction. According to the new pattern, all negotiating countries would agree on a formula of tariff reduction which is to be applied to all products in the negotiation list, save the case of high tariff disparity to protect those countries whose tariff rate regarding a specific product is before the reduction already relatively much lower than those of other countries.

With the political pressure for protection increasing and tariffs being gradually reduced, the use of non-tariff trade barriers has been intensifying. Several codes of conducts regarding various use of non-tariff trade barriers were produced in the Kennedy and the Tokyo rounds. These codes are intended to be implementation of the main articles in the General Agreement dealing with these non-tariff trade barriers. However, contracting parties of the GATT are not necessarily signatories of these codes. Individual codes also set up their own committees to oversee the operation of the codes.

In 1973, the arrangement regarding textile trade was incorporated into the GATT system. The Multifiber Arrangement of 1973 is a sectoral safeguard system specifically applied to textile trade. It allows discriminatory safe-duard measures, contrary to the basic principles of non-discrimination and reciprocity and is generally regarded as an exception to the general rules of the GATT.

When disputes arise, the GATT encourages disputing countries to settle their difference through consultation or conciliation. When consultation or concilation takes place at the GATT level, the committees and the Contracting Parties would act as concilators, or provide assistance to the parties in dispute. When the dispute becomes irreconcilable, a panel composed of experts on the issue in dispute would be appointed to investigate the case. Parties in dispute would still be encouraged to settle their difference by mutually acceptable solution before the Contracting Parties or the committee, according to the panel's report, makes recommendation on the resolution of the case. If one party fails to comply with the recommendation, withdrwal of concessions to trade with that party by the other party would be authorized.

To bring a case to the GATT for adjudication, there shall be a cause of action. The main cause of action is the notion of nullification or impairment of benefits accruing to the parties under the GATT law. Violation of the GATT rules itself is a prima facie case of nullification or impairment. A non-violation nullification or impairment is much more difficult to establish. In establishing such a case, there shall be demonstration of the existence of benefits, of reasonable expectation that the benefits will not be nullified or impaired, and of damage. The major test for a case of nullification or impairment is whether the balance of economic advantages resulting from trade negotiations has been damaged.

(A) Introduction to Pre-1979 Subsidy Law under the GATT

Subsidies are dealt with in article XVI of the General Agreement.*1 Any contracting party grants a subsidy which operates directly or indirectly to increase exports or to reduce imports is required to notify the Contracting Parties. The extent and nature of the subsidy, the estimated effects on the quantity of the affected product, and the circumstances making the subsidization necessary, should be revealed in the notification. In the case that such a subsidization causes or threatens to cause serious prejudic to the interest of other contracting parties, the contracting party, should upon request consult with other parties affected or the Contracting Parties the possibility of limiting the subsidization. If such consultation fails to reach a satisfactory solution, the Contracting Parties, according to Article XXIII, may authorize other parties to suspend the application of concessions or other obligations to trade with the practicing party.

In 1955, some additional provisions on export subsidies were added as Section B of Article XVI.*2 These provisions took a harder line with regard to export subsidies. There is explicit recognition that export subsidies may have various adverse effects on the interests of other countries. Export subsidies to primary products are given more tolerence and allowed to the extent that a subsidization would not lead to the practicing party obtaining more than an equitable share of world export trade in the subsidized primary product. In contrast, export subsidies to non-primary products are prohibited if they result in sales for exports at prices lower than those charged in the domestic market. The prohibition only applies to those seventeen countries which have accepted the declaration giving effect to it.

There are also several supplementary rules.*3 Exemption of an exported product from domestic taxes or duties or the remission of such taxes or duties is not considered as a subsidy. Multiple exchange rate practices not violative of the IMF Agreement are not prohibited. Primary products are defined as products of farm, forest, or fishery, or any mineral, in their natural forms or having been processed as customarily required for marketing. A system for stabilizing the domestic prices of primary products independently of the movements of export prices will not be considered to involve a subsidy on exports even though it results at times in lower export prices. This rule is conditional on : (1) it also results in higher export prices, and (2) it is not designed to stimulate exports unduly. However, the system should be considered as a subsidy practice if there are government funds involved.

(B) Subsidies after the Tokyo Round

In 1979, the Multilateral Trade Negotiations (MTN, also known as Tokyo Round) produced the Agreemenr on Interpretation and Application of Article VI, XVI, and XXIII *4 (the MTN Subsidy/Countervailing Duty Code, hereafter the Code) to cope with the increasing use of subsidy measures. The following discussion will include the Code as well as pre-MTN anti-subsidy practices.

(1) Definition of Subsidy

The GATT Panel of Experts on Subsidies in its 1961 report on the operation of the provisions of Article XVI took the view that it was neither necessary nor feasible to seek an agreed interpretation of what constitutes a subsidy and that the lack of a precise definition had not in practice interfered the operation of Article XVI.* 5 However, from the Panel's previous report on the notification of subsidies, the non-exclusive list of export subsidy practices developed by a working party in 1960 and incorporated into the Code, the non-exclusive list of subsidies other than export subsidies provided in the Code, and subsidy cases adjudicated in the GATT, several points can be made with regard to the definition of subsidy. First, there should be involvement of government action. The GATT only concerns about governmental actions and is not intended to deal with actions by private persons. A group of producers may voluntarily tax themselves to subsidize their exports. Such actions cannot be considered as subsidy practices within the meaning of Article XVI.* 6 The Code further provides that the term "subsidies" shall include "subsidies granted by any government or any public body within the territory of a signatory." * 7 An interesting comparison can be made with the counterpart of this provision in the U.S. countervailing duty law which allows countervailing duties to be applied to imports which receive bounties or grants from any country, dependency, colony, province, or other political subdivision of government, person, partnership, association, cartel or corporation.* 8 The Code in dealing with the definition of subsidy does not explicitly mention whether the term "government" includes authorities of customs unions. In regulating settlement of disputes arising from subsidy practices, it says the term "governments" is to be understood to mean governments of all member countries in cases of customs unions.*9 However, in the final provisions of the Code, it is provided that the EEC should be considered as a contracting party and the competent authorities of the EEC a government.*10 Thus, subsidies granted by the EEC Commission may fall within the Code's concern, but those by the authorities of other customs unions do not. A government may grant subsidies by entrusting a private body the function of taxation and subsidization with the rsult that the pratice would in no real sense differ from those formally followed by the governmentm.*11

Second, there should be involvement of government funds. A government may fix the domestic price of a commodity at above the world price level without resort to a subsidy. It can fix by law a minimum price which is maintained by quantitative restrictions or flexible tariffs or similar charges.*12 Such a government action is to be dealt with by other Articles of the General Agreement but not within the scope of Article XVI. Involvement of government funds can be in several forms other than outright grants. In the case of taxation, involvement of government funds can be in the form of exemption or remission of taxes, or special depreciation allowed in the calculation of tax bases. Moreover, government provision of goods or services, though at terms more favourable than commercial terms, should not be considered as a subsidy practice, if the government incurs no loss in such an operation.*13

(2) Scope of Article XVI and the Code

The General Agreement does not explicitly define the scope of Article XVI. Article XVI requires all contracting parties to notify the Contracting Parties all subsidy practices which operate "directly or indirectly to increase exports of any product from,or to reduce imports of any product into", the subsidizing countries. Thus, subsidies that conform with the above description may be within the scope of the substantive rules of Article XVI. There is however an overlap of the scopes of Article XVI and Article III. Article III prohibits any discriminatory treatment aimed at protection of domestic production except, among others, the payment of subsidies exclusively to domestic producers.*14 " The payment of subsidies exclusively to domestic producers " was so narrowly interpreted in the Italian Discrimination against Imported Agricultural Machinary case as to exclude subsidies granted to purchasers of domestically produced machinary.*15 Thus, these subsidies are to be governed by Article III as well as by Article XVI. The Code does not explicitly define the scope of its coverage in order to clarify the problem of overlap. The only clue one can find in this regard appears in a note regarding the definition of countervailing duty which says ' the term "countervailing duty" shall be understood to mean a special duty levied for the purpose of off-setting any bounty or subsidy bestowed directly or indirectly upon the manufacture , production , or export of any merchandise, as provided for in Article VI:3 of the General Agreement '.*16 (emphasis added) Thus, subsidies other than those bestowed upon manufacture, production, or export of any merchandise, such as the one in the Intalian Machinery case, are to be excluded from the application of countervailing duty law. If this definition can be applied to the Code as a whole,i.e. to the sections regarding subsidy practices and dispute settlement as well, the problem of overlap will be eliminated, and Article III will have the sole jurisdiction on subsidies to domestic purchasers. Such a definition would penalize the use of subsidies to domestic purchasers to boost import-competiting industries, because under Article XVI and the Code such use is not prohibited if it does not result in certain degree of adverse effcts. On the other hand, they are prohibited under Article III without regard to their effects on trade.*17

(3) Notification

As mentioned previously, contracting parties shall report all subsidy practices which operate to increase exports or reduce imports.

" To increase exports " includes the "concept of maintaining exports at a level higher than would otherwise exist in the absence of a subsidy".*18 The same interpretation applies to "to reduce imports" as well. Thus, the criterion in deciding the notifiability of a subsidy is what would happen in the absence of the subsidy.* 19 An important assumption is that a subsidy which provides an incentive to increase production will in the absence of offsetting measures, either increase exports or reduce imports.* 20 The duty of self-reporting can hardly be expected to be complied with, when a subsidizing country realizes that the information it submits to the Contracting Parties will possibly be used as the basis for the taking of counteractions by other contracting parties. To remedy this defect, the Code provides that other contracting parties have the right to request for information on the subsidy concerned.

(4) <u>Substantive General Obligation Regarding Subsidies</u>

Article XVI does not explicitly specify the general obligations regarding the use of subsidies, although it specifically stipulates obligations regarding the use of export subsidies and export subsidies to primary products. The Code concretes the general obligation implied in Article XVI,* 21 incorporates the general obligation stipulated in Article XXIII and VI, and transforms them into general obligation regarding the use of a subsidy. According to the Code, signatories agree "to seek to avoid causing, through the use of any subsidy,:

> (a) injury to the domestic industry of another signatory;
> (b) nullification or impairment of the benefits accruing directly or indirectly to another signatory under the General Agreement; or
> (c) serious prejudice to the interest of another signatory."* 22

The word "injury" means material injury to a domestic industry, threat of material injury to a domestic industry, or material retardation of the establishment of such an industry.*23 A country whose interest is adversely affected may seek remedy through the multilateral dispute settlement scheme provided in the Code or through the self-defence mechanism of countervailing duties. The determination of injury is stipulated in the Code dealing with countervailing duties and shall be discussed in the next chapter. A country whose benefits under the GATT are nullified or impaired or whose interest is seriously prejudiced can only seek remedy through the multilateral dispute settlement scheme.

(a) Nullification or Impairment of Benefits Accruing to Signatories

The phrase "nullification or impairment" originally appears in Article XXIII as a precondition for the invocation of the GATT dispute settlement mechanism. After the Tokyo Round negotiations, the mechanism was incorporated into each code of conduct dealing with non-tariff trade barriers. Nullification or impairment is, according to the precedent laid down in the *Uruguay* case,*24 presumed to exist when there is an infringement of obligation stipulated in the General Agreement. It is up to the contracting party against whom a complaint was brought to the GATT to rebut the charge. A *prima facie* case of nullification or impairment would *ipso facto* require consideration of whether the circumstances are serious enough to justify authorization of retaliation to the complaining country by the Contracting Parties, or in the case of subsidy, by the Committee on Subsidies and Countervailing Measures.

When the nullification or impairment does not arise from a breach of obligation, a complaining country should provide a detailed account to domonstrate the justification of its claim. To establish a case of non-violation nullification, there are three requirements to be met: (1) there exists a reasonable expectation that the benefits under the GATT would not be nullified, (2) the benefits should be specific and clearly defined, and (3) the trade effects of the practice in issue should be serious enough.

(i) Reasonable Expectation

In the determination of reasonable expectation, the GATT adjudicating bodies tended to base their rulings on specific conducts of the defending country which have the effect of inducing an expectation. In the leading Australia Subsidy case, the Working Party held that the removal of an existing subsidy on one type of fertilizer, while maintaining some other subsidy on another fertilizer which existed in parallel with the first subsidy before its removal, would be beyond the reasonable expectation that either of the subsidies would not be removed before the removal of the other one, and the competitive relationship of the products receiving the subsidies would not be changed.*25 This is because of the following four considerations:

> " (a) The two types of fertilizer were closely related;
> (b) Both had been subsidized and distributed through the same agency and sold at the same price;
> (c) Neither had been subsidized before the War, and the war-time system of subsidization and distribution had been introduced in respect of both at the same time and under the same war power of the Australian Government;
> (d) The system was still maintained in respect of both fertilizers at the time of the 1974 negotiation."*26

These considerations are detailed and specific, and the ruling was so limited that the introduction of a new subsidy, in contrast to the removal of or the maintaining of an existing subsidy, such as those in the present case, would lead the Working Party to rule otherwise. In the 1954-1955 Review Section, the Working Party extended the ruling a step further in regard to domestic subsidies. It was stated that a contracting party may be presumed

"to have a reasonable expectation, failing evidence to the

> contrary, that the value of concession will not be nullified or impaired by the contracting party which granted the concession by the subsequent introduction or increase of a domestic subsidy on the product concerned. " (emphasis added)*27

The extension is limited as it did not cover competitive substitute products, even though it is highly possible that subsidies on these products may nullify or impair the value of concession that foreign imports received in the previous round of tariff reduction negotiations. This raises the suspicion that the Working Party by stressing "the product concerned" in fact suggested that the exitence of bad faith be essential for the establishment of a resonable expectation.*28 In the Norwegian Sardin case,*29 an assurance given in the previous negotiation that a product would not be treated less favourably was a sufficient inducement of a reasonable expectation. This was so even without a customary written confirmation. In the German Duties on Starch case, an offer to negotiate tariff reductions on some starch products would give rise to a reasonable expectation that the tariffs would be eventually lowered.*30 From these rulings, one can perceive that it is not sufficient to base a claim on the mere fact that the complaining country is unable to anticipate. It must be supported by evidence to the effect that the inability to anticipate is due to certain conduct of the defending country, and the defending country is in bad faith in introducing new or changing policies.

(ii) Benefits Accruing to Parties under the GATT

The purpose of Article XXIII is to maintain the balance of economic advantages resulted from previous exchanges of concessions, i.e. the economic substance of the princple of reciprocity. It is difficult, if not impossible, to quantify the economic advantages a country gained from the concessions made by another contracting party. The only criterion in assessing whether reciprocity has been reached is a country's own satisfaction at the result of the exchange of concessions. Since there is hardly any objective standard, the more specific the concessions, the less burdensome the determination of whether the balance of economic advantages has been affected by a subsequent action or inaction of a defending country. In the Australia Subsidiy case the benefit nullified by the change in subsidy policies was the duty-free treatment granted by Australia to Chile on the fertilizer regarding which subsidies were maintained while subsidies on the other fertilier were removed.*31 In the Norwegian Sardine case, the benefit in issue was the assurance that Norwegian sardin products would not be given less favourable treatment than Portuguese-type sardin products.* 32 In the German Duties on Starch case, it was the promised tariff reduction that was nullified by Germany's failure to implement the tariff reduction.* 33 In the EEC Minimum Import Prices, Licensing and Surety Deposits case, the benefit which was nullified by the EEC program of minimum prices, licensing, and surety deposits for certain processed fruit and vegatable was the tariff concession made by the EEC to the imports of tomato concentrates from the U.S..* 34

All the benefits concerned in the above mentioned cases are tariff-related concessions. The benefits for the purpose of Article XXIII can also arise from non-tariff concessions. A contracting party when assuming an obligation regarding non-tariff matters under the GATT, such as the obligation of refraining from the use of quota, would expect its action to be reciprocated by those of others, and the benefits resulting from others' compliance with GATT rules on the obligation would not be nullified. This kind of benefit can be nullified not only by non-compliance with GATT rules but also by non-violation actions.

Non-violation nullification can be resulted from the application of the so-called "grandfather clause", waivers of obligation for special circumstances, such as waivers in the case of customs unions.* 35.

If one applies the concept of contract law to the two kinds of benefit mentioned above, they are equivalent to considerations in the making of a contract. In some cases the contracts in issue are legitimately valid, but they may be considered not binding by courts because they may result in inequity between the parties. The same can be applied to the present discussion of nullification of benefits, when the exchange of concessions is subsequently found to be inequitable.*36 Although the balance of advantages is mainly to be judged by subjective criteria, it is still possible to establish a case of nullification by employing objective criteria when the exchange apparently appears to be inequitable or most of the contracting parties of the GATT agree so. The first case basing on the benefit of equity was brought to the GATT by Uruguay. The Uruguay Government listed 562 restrictions imposed by 15 countries in its claim under Article XXIII.* 37 It did not follow the pattern of previous cases, and refused to supply data and to indicate what specific benefits that were nullified. The only cause of action given was "the general difficulties created for Uruguay by the prevalence of restrictive measures affecting its exports" and "the resulting inequity in the terms of trade which temperate products participated in world trade". The Panel found itself unable to adjudicate the case, lacking the same kind of information as available in previous cases. It did partially resolve the case by sorting out some of the restrictive measures which were inconsistent with the GATT rules and therefore was able to evade the problem of specifying the benefits that were nullified.* 38 As to those non-violative measures, it laid down the precedent that detailed submissions were essential for a judgement to be made in these regards.* 39 When dealing with the issue of "general difficultes" and "inequity" in trade terms, the Panel said that "it was not charged with the examination of broader issues falling outside the purview of Article XXIII".* 40

The benefits claimed by the Uruguay Government to be nullified are in fact the expectation that the exchange of concessions either tariff-related or non-tariff-related, will not result in an inequitable balance of economic advantages, and the benefit of equity specially accruing to developing countries. The first kind of inequity applies to all contracting parties of the GATT, while the second kind only applies to the developing countries. The problem of inequity is not explicitly mentioned in the General Agreement, and the legislative history of Article XXIII does no preclude the possibility of a case of nullification of benefit basing on the notion of equity.* 41 In so far as the benefit of equity specially accruing to the developing countries is concerned, in 1964 a new chapter on trade and development was added to the General Agreement, emphasizing the trade interest of the developing countries.* 42 This involves preferential market access and other preferential treatment that should be accorded to the developing countries. Had the uruguay case been brought to the GATT after 1964, Uruguay could have been able to base its case on a more solid ground by claiming the benefit of equity embodied in the new chapter was nullified, although there was no breach of terms of the exchange of concessions.*43

The reason that the Panel in the Uruguay case refused to consider the problem of equity may be that the Panel felt that the extent to which an exchange of concession could be considered as inequitable should be decided through multilateral consultations which are the main policy-making mechanism of the GATT. It is true that whether a specific exchange of concession is inequitable in the sense that the developing countries should be accorded special considerations is a policy matter and should be decided through multilateral consultations. But there are cases where the inequity in issue is not so much of a policy matter. The inequity may only arise from imbalance of economic advantages, because the negotiators were unable to anticipate the effects of a concession, in part owing to the inadequacy of the existing forecasting techniques, or that the existing legal techniques were unable to reflect the balance of economic advantages that the negotiators had in mind. If the countries concerned are limited in number and the trade interest involved is limited in scope, the inequity can be adequately handled by the Panel which can settle the case by requiring the parties to adjust their terms of exchange or authorizing countermeasures to offset the economic disadvantage. However, when the inequity exists among groups of countries and the trade interest involved is far from limited, the dispute settlement mechanism of Article XXIII may appear inadequate. The remedy would require changes in the GATT rules concerned (common terms of exchange). This would in turn require multilateral consultations and renegotiation of rules.

(iii) Reasonable Expectation Revisited

Early cases of non-violation nullification strictly stuck to the rule of reasonable expectation. The expectation should be induced by specific conducts of the defending country. Meanwhile, the benefits involved in those early cases were limited to specific concessions regarding a limited number of products. This line of cases was necessarily influenced by the emphasis on tariff reductions and the method of negotiation in the early stage of the GATT. Negotiations on a product-by-product and country-by-country basis are very much like negotiations of contracts between every two contracting parties of the GATT, guided by the principle of reciprocity. The terms of exchange of concessions may vary from countries to countries and from product to product. The search for specific conducts in the determination of reasonable expectation is in essence to examine the circumstances under which concessions were exchanged and consequently to define the substance of the terms of the exchanges. From the Kennedy Round onwards, the pattern of tariff reduction has been changed from product-by-product and country-by-country to across-the-board cuts. According to the across-the-board method, all contracting parties of the GATT agree on a reduction formula to be applied to all exchanges, except those cases of wide tariff disparity.* 44 The characteristic of such a package deal is that the terms of exchange are arbitrarily determined without regard to the existing conditions of trade in specific products between any two countries. The cut-off of the link between the terms of exchange and the underlying circumstances of negotiation makes it unnecessary to define the substance of the terms by reference to the underlying circumstances. This means the requirement of reasonable expectation is no longer necessary.

The same can be said about exchanges of non-tariff-related concessions. Negotiations of such exchanges are similar to those of the across-the-board tariff reduction, which involves negotiation of a rule regarding a specific non-tariff trade practice, participated by all contracting parties. Such multilateral activities do not involve (at least theoretically) bilateral trade-offs which are the main concerns of the requirement of reasonable expectation. In the case of nullification of equity, the need to prove reasonable expectation is even weaker, because the issue in dispute is usually not what the substance of the terms of exchange, but whether the exchange has resulted in inequitable balance of economic advantages.

The above mentioned development seemed to be endorsed by recent cases. In the EEC Minimum Import Prices, Licensing, and Surety Deposits case,*45 both parties produced no arguments on the issue of reasonable expectation and the Panel, unlike in previous cases, did not investigate the issue and dismissed the case on the ground of insufficient trade effects. In the following EEC's Refunds on Exports of Sugar , the Panel again did not mention the requirement of reasonable expectation, and dismissed the claim of non-violation nullification because the complaining Australia made no detailed submission as to exactly what the nullified benefits were.*46 The confusion arising from these rulings is whether the Panel regarded it unnecessary to investigate the issue of reasonable expectation because of the above mentioned development or because the complaint failed to fulfill other requirements. The clarification of such confusion shall wait for future development.

(iv) Trade Effects and Causal Link

With regard to the sufficiency of trade effect and causal link in the case of non-violation nullification, the GATT panels have not developed a consistent standard. In the Norwegian Sardin case,*47 the Panel found that after the German Government failed to keep the promise not to upset the competitive relationship between Norwegian and Portuguese imports of sardin, Norway suffered substantial decrease in its exports of sardin to Germany. The Panel also found that, given the trade statistics available, it is impossible to reach a definitive conclusion regarding the causal link. Despite of this, the Panel concluded that the value of concession received by Norway in the Torquay negotiations was substantially reduced and therefore it had suffered an impairment of a benefit accruing to it under the General Agreement. The substantial standard seemed maintained in the French Assistance to Exports of Wheat and Wheat Flour.*48 In that case, the Panel found that, following French Government's granting subsidies to its exports of wheat and wheat flour, its market share in the Southeast Asia markets grew substantially (from 0.7% in 1954 to 46% in 1958), whereas that of Australia in the same area fell substantially (from 83% in 1954 to 37% in 1958). Although the Panel felt it difficult to quantify the displacement effect of the French subsidies on Australian exports, it nevertheless found it clear from the above statistics that French supplies had to a large extent displaced the Australian supplies. This, together with the finding that the export subsidies had resulted in France having more than an equitable share of world export trade, led to the conclusion that the French practice had nullified the benefit accruing to Australia that its exports would not face subsidies going beyond the equitable share limitation. The French Subsidy case is a clear case with wide changes in market shares and a strong causal link. In contrast, the following Italian Machinery *49 case is a relatively weaker one. In the five year span after the introduction of credit facilities to the purchase of Italian agricultural machinery, total imports of tractors remained at a more or less stable level except the last two years in which there was a significant falling off of imports. Imports from the complaining country, the U.K., followed the same trend in the first part of the five-year period, but the decline was more marked in the latter part. Meanwhile, the statistics showed that in terms of registration, the share of imported tractors in the total registration steadily decreased, although the absolute numbers were not very large. The Panel also found that the falling of imports, in particular from the U.K., could not be entirely attributed to the credit facilities, and that the credit faciliies probably influnced a number of purchasers. Basing on these facts, the Panel therefore recommended the Italian Government to modify its credit facilities so as to permit a fair choice between purchases of tractors of domestic and of foreign origin.

The only instance where the Panel dismissed the case on the ground of insufficient trade effect is the EEC Minimum Import Prices, Licensing and Surety Deposits case.* 50 The Panel in that case not only found that the EEC import certificate and associated security system were not inconsistent with Article VIII,* 51 but also ruled that the operation of the system had no trade effects which could be considered as a nullification or impairment within the meaning of Article XXIII. This is because: (1) the imports in issue, i.e. tomato concentrates from the U.S. only accounted for 0.1% of the EEC total imports, and exports to the EEC represented about 1.8% of total U.S. exports of the product; (2) that in the years following 1962 when the concession had been granted to the U.S., the U.S. did not develop the opportunity and its exports to the EEC has always stood at an insignificant level, means the concession in effect benefited the U.S. insignificantly; and (3) the charges associated with the system did not exceed 0.005% of the minimum prices imposed on imports of tomato concentrates.* 52 Since the present case is an extremely weak one, it provides no important information as to the extent to which a case of non-violation nullification can be considered valid.

(b) Serious Prejudice to the Interest of Another Signatory

Under the design of the Code, a signatory whose interest is seriously prejudiced by the use of a subsidy by another signatory can also invoke Article XXIII-style dispute settlement scheme provided in the Code. The EEC's Refunds on Exports of Sugar * 53 is the first instance in which a claim was made on the ground of serious prejudice. Although the Panel was unable to establish the causal link between the increase in EEC's market share and the loss of market share of the complainant Australia, it found that the EEC system of refunds on exports of sugar had contributed to depressed world sugar prices and indirectly caused serious prejudice to the interest of Australia. This is because: (1) sugar prices had been very sensitive to the balance between supply and demand; (2) the refund was made to cover the difference between the higher EEC internal prices and world market prices, and in the period under consideration the refunds tended to exceed the difference; (3) the EEC exporters traditionally covered more than half of the world market for white sugar; (4) the sharp increase in the refunds coincided with a sharp decline in world market prices; and (5) the availability of exportable surplus of sugar combined with the possibility of unlimited amount available for refunds may well have had a depressing effect on world market prices for sugar. In addition to the depressing effect on world market prices for sugar, the system also constituted an effective source of unceratinty in world sugar markets and therefore a threat of serious prejudice to the interest of Australia because the system did not have an effective limitation on either production, price or amount of refunds.

(c) Quantitative Guidelines for the Determination of Trade Effects

Although the Code does not specify the level of trade effects necessary to establish a case of nullification or impairment or serious prejudice, it provides some qualitative quidelines for the determination of trade effects.* 54 It first repeated the well established rule that nullification can arise from violation of GATT provisions. Under such circumstances, there is certainly no need to investigate the issue of trade effects, since a _prima facie_ case can be presumed to exist as a result. The adverse effects necessary to establish a case of non-violation nullification or serious prejudice may arise through

> " (a) the effects of the subsidized imports in the domestic market of the importing signatory,
> (b) the effects of the subsidy in displacing or impeding the imports of like products into the market of the subsidizing country, or
> (c) the effects of the subsidized exports in displacing the exports of the like product of another signatory from a third country market."*55

It is noteworthy that the provision of displacement in a third country market does not apply to subsidies on certain primary products which are to be governed by the rule of "more than an equitable share of export trade" provided in Article 10 of the Code.

(d) <u>Material Injury, Nullification or Impairment, and Serious Prejudice</u>

A question should be asked at this stage is whether there is any difference between the trade effects necessary to establish a case of nullification or impairment, material injury and serious prejudice. The only possible one is the difference in the levels of trade effect, because the adverse effects necessary to demonstrate nullification or impairment and serious prejudice may arise through the same circumstances, one of which,i.e. the effect on the domestic market of the importing country, includes the situation of injury to a domestic industry. Whether the level of trade effect required for each case is actually different is difficult to answer. As mentioned previously, no clear guidance has been developed by previous cases, nor does the Code provides any guidance. If there is no such difference in the drafters' minds, what is the intention in providing three alternative remedies? The answer may be that such an arrangement would increase the opportunity of a successful and effective anti-subsidy action. If a subsidy has caused injury to the domestic industry of an importing country, the importing country can take action either through the use of countervailing duties or through the multilateral dispute settlement scheme provided in the Code. When there is violation of provisions of the Code or articles of the General Agreement, a case of nullification or impairment can be easily established by use of the convenient tool that the necessary adverse effects are presumed to exist.*56 Otherwise, invocation of the serious prejudice clause can avoid the cumbers~~on~~me task of demonstrating the benefits claimed to have been nullified and sometimes the existence of reasonable expectation.

(5) <u>Specific Substantive Obligation: Export Subsidies on Products Other Than Certain Primary Products</u>

The Code following Article XVI prohibits the use of export subsidies on products other than certain primary products. Certain primary products are defined in the Code in the same way as in Article XVI with the deletion of mineral products. *57 As refraining from the use of export subsidies is made an obligation under both the Code and Article XVI, those adverse effects necessary to demonstrate nullification or impairment are presumed to exist, when the failure to carry out such an obligation is determined by the Committee on Subsidies and Countermeasures.*58 The presumption is rebuttable, and is limited to a case of nullification or impairment. If an importing country is seeking remedy under the material injury or the serious prejudice clause, the presumption will not apply. The Code's presumption with regard to the use of an export subsidy on products other than certain primary products is more confined than the presumption under Article XXIII. Under Article XXIII, whenever there is an infrigement of GATT obligation , a complaining party can establish a <u>prima facie</u> case of nullification or impairment without demonstrating what the benefits are and how they have been nullified or impaired by the resulting effects of the subsidy practice in question. The Code, however, only presumed the existence of adverse effects in the case of export subsidies on products other than primary products, and therefore the complaining party would have to bear the burdern of demonstrating the benefits and other related issues. Such a rule of presumption would make the dispute settlement scheme provided in the Code useless in so far as nullification or impairment is concerned, because a complaining country may well seek remedy under Article XXIII rather than provisions of the Code. The case will therefore be dealt with by a panel appointed by the Contracting Parties rather than a panel appointed by the Committee on Subsidies and Countermeasures.

The Code is silent on the requirement of dual pricing in the determination of the legality of an export subsidy on products other than primary products. In the case of Article XVI, those contracting parties accepting the Declaration Giving Effect to Article XVI:4 only agree to refrain from export subsidy practices that result in dual pricing. One may argue that the Code in providing that signatories " shall not grant export subsidies on products other than certain primary products",* 59 intends to impose more stringent control on the use of export subsidies. Export subsidies on products other than certain primary products are illegitimate *per se* no matter whether they result in dual pricing. There are however three arguments that may gear the conclusion towards the opposite direction. First, in an early draft of the Code the phrase "whether or not such subsidies result in dual pricing " was added immediately after the phrase "...shall not grant export subsidies...". the deletion of the phrase from the final draft at least shows there is no positive intention to abandon the dual pricing requirement. Secondly, in the case that the Code does not explicitly provide otherwise, the rule provided in Article XVI or its supplementary provisions should be deemed abolished. Thirdly, the Panel of the DISC and the the Income Tax Practice by Some European Countries cases made it clear that the absence of the requirement of dual pricing in the illustrative list of export subsidies did not mean that dual pricing was no longer required.* 60 Instead, the listed export subsidy practices were presumed to result in dual pricing.

If dual pricing is still required, there will be several difficulties in its application. First, there will be the difficulty in making a comparison. Dual pricing in the case of subsidy is defined as "... the sale of ...the subsidized product for export at a price lower than the comparable price charged for the like products to buyers in the domestic market."* 61 Experience from antidumping administration teaches that there are enormous complexities in the determination of prices and in making adjustments for the purpose of comparison. If it proves inappropriate to adopt those established guidelines in antidumping administration, the Committee on Subsidies and Countermeasures will have to provide its own guidelines. Meanwhile, the requirement of dual pricing may also bring more complexities to the already complicated anti-subsidy administration. However, the complexities can be greatly minimized by the interpretation that export subsidies included in the illustrative list are presumed to result in dual pricing. This is even more so after the Working Party in its Report on Export Inflation Insurance Scheme extended the presumption to all export subsidies, no matter whether they are included in the illustrative list.* 62 Secondly, the dual pricing criterion may prove inadequate to regulate export subsidy practices. Export competitiveness can be enhanced through subsidization by non-pricing methods such as better sales services, more intensive advertising and more product guarantee.*63 Improved cash flow, product development, and the achievement of economies of scale for exporting firms may also serve the same purpose.*64

Definition of Export Subsidy

The Code does not provide a general definition of export subsidy but provides an illustrative list of export subsidies. The list is non-exclusive and is discussed in the following.

(a) Border Tax Adjustments

(i) General Definition

The Code follows the classic assumption that indirect taxes are fully shifted forwards and direct taxes fully backwards. Thus, the following practices are considered as export subsidies.

> "The full or partial exemption, remission, or deferral specially related to exports, or direct taxes or social welfare charges paid or payable by industrial or commercial enterprises."*65

> "The allowance of special deductions directly related to exports or export performance, over and above those granted in respect of production for domestic consumption, in the calculation of the base on which direct taxes are charged." *66

> "The exemption or remission in respect of the production and distribution of exported products, of indirect taxes in excess of those levied in respect of the production and distribution of like products when sold for domestic consumption."*67

Direct taxes include taxes on wages, profits, interest, rents, royalties and other forms of income, and taxes on the ownership of real property.*68 Indirect taxes are sales, excise, turnover, value added, franchise, stamp, transfer, inventory and equipment taxes, border taxes, and all taxes other than import charges and direct taxes.*69 Tax deferral does not necessarily constitute an export subsidy, especially when appropriate interest charges are collected.*70. In the calculation of taxes, prices charged for sales to foreign enterprises, which are under the exporting enterprises's control or under the same control as the exporting interprise, should be the prices charged between independent enterprises at arm's length.* 71

The definitional problem in regard to border tax adjustment was discussed in detail in the reports of the panel on the U.S. DISC legislations of France, Belgium, and the Netherlands.* 72 The main characteristics of the DISC legislation are that it allows a domestic corporation to elect to be a DISC, provided several requirements are fulfilled, and that half of the DISC's earning is deemed distributed to its shareholders and is taxable to those shareholders as dividends, whereas the retained earning is not subject to federal income tax until one of the following events occurs: (1) there is an actual distribution of the retained DISC earning, (2) the DISC is liquidated, (3) a shareholder disposes of the DISC stocks, and (4) the corporation fails to qualify as a DISC for the taxable year.* 73 The DISC legislation was accused by the EEC and Canada of providing subsidies to the U.S. exporters on the following grounds. Firstly, the DISC scheme provided no rule which in practice could prevent the tax deferral from being maintained indefinitely, and this amounted to total exemption from direct federal corporate taxes for one half of the profits of a DISC.* 74 Secondly, even if the tax deferral was to end either in exceptional circumstances or through the elimination of the DISC system, the exemption of the compound interest on the deferred tax still constituted an export subsidy.* 75 Thirdly, the two options other than the arm's length rule for inter-company pricing between related buyers and suppliers provided in the DISC scheme were alleged to be inconsistent with the arm's length principle under which the allocation of profits from inter-company transactions between related parties is determined by competition in the marketplace. Under these two options, the profit of a DISC could be either 4% of its sales receipts, or 50% of the combined taxable income of the DISC and its related suppliers. Thus, U.S. manufacturing corporations were encouraged to establish DISCs as their sales subsidiaries or sales agents, because under the DISC scheme they could choose any of the two options which would allow more profits to be distributed to the DISC subsidiaries or sales agents than the arm's length rule.* 76

The U.S. in response to the above accusation advanced the following arguments. Firstly, the DISC legislation only provided for a deferral rather than an exemption of corporate income tax, and therefore was not covered by the illustrative list of export subsidy. Consequently, the DISC legislation should not be considered as providing export subsidies without investigating its economic effects.* 77 Although a tax deferral extended for a sufficient period of time, the existence of uncertainties as to the duration of and the amount of benefits that could be obtained from the DISC scheme negated any analogy between the deferral under the DISC legislation and the exemption of tax.* 78 Uncertainties arised in part from the difficulty in meeting the qualifying test, because to qualify as a DISC would require exports growing at an increasingly rapid rate. There also existed uncertainties due to the constant threat of the repeal of the DISC legislation. Secondly, tax deferral was necessarily an aspect of any tax system, because no system could ensure collection of tax as accrued.* 79 Thirdly, with regard to inter-company pricing, in most cases a 50-50 split of profits between a parent and its DISC was chosen and therefore a 75-25 allocation of profits between those currently taxable and those subject to tax deferral was followed. In contrast, some GATT member countries provided for a 50-50 allocation of profits between those taxable and those subject to complete exemption.* 80

The Panel took the position that the DISC legislation constituted a partial exemption of corporate income tax, not because the tax deferral was granted for an indeterminate period, but because the deferral was not accompanied by interest levies.* 81 The Panel also held that the rules regarding inter-company pricing in the DISC legislation could influence the size of the exemption.* 82

In addition to the definitional problem, there are three issues regarding the DISC case to be discussed further. The U.S. in defending its DISC legislation argued that the legislation was intended to correct distortions resulted from the application of the territoriality principle embodied in the tax legislations of France, Belgium and the Netherlands.* 83 The Panel rejected this argument because one distortion could not be justified by the existence of another one.* 84 The Panel could have based its decision on legal considerations and made the decision more legally convincing. What the U.S. argued about was that the DISC legislation was a countervailing or retaliatory measure intended to offset the competitive effect of the territoriality principle. It is true that the use of countervailing or retaliatory measures is allowed under the GATT to offset the effect of a distortive practice, but such use should be authorized by the GATT rules or the Contracting Parties in order to prevent abuse. The DISC scheme is not legally allowed, because it did not go through the necessary legal process under the GATT law.

The U.S. also argued that since the application of the territoriality principle had never been regarded as subsidies, those countries adopting the principle could not have a reasonable expectation that the DISC legislation was contrary to the subsidy rules of the GATT.*85 There thus existed a consensus that both the territoriality rule and the DISC legislation did not violated the GATT obligations regarding subsidies, because the Vienna Convention on the Law of Treaties stipulated that subsequent practices of parties to a treaty represented a proper reference to its interpretation.*86 The Panel did not consider that there existed such a consensus only because tax practices had been in force for some time without being subject to complaints.*87

Most interestingly, in calculating the trade effects of the DISC legislation, the Panel although following the assumption that direct taxes were fully shifted backwards and considering a partial exemption of direct taxes as a subsidy, took the position that the effect of such a subsidy was not necessarily fully reflected in the profit levels of the benefit-receipients only.*88 The effects were also reflected in prices and sales eforts such as better advertising.

Another issue facing the Panel was the legitimacy of the territoriality principle followed by France, Belgium, and the Netherlands in their handling of international double taxation.*89 According to the principle as applied by France, French companies are taxes solely on profits made by enterprises operating in France and on profits taxable by France under international double taxation agreements with other countries. Profits generated by undertakings, either branches, subsidiaries or associated companies, operated abroad, are exempted from French taxation. In order to prevent the establishment of fictious corporations located abroad, all corporations which have an effective management headquarter in France are taxable in France. Dealings between associated companies should be governed by the arm's-length rule. On the other hand, a French company is not entitled to any credit for taxes paid to foreign governments and cannot deduct its losses in foreign adventures.

The French practices were objected by the U.S. on the following grounds. Firstly, the tax exemption was extended to foreign-source income from activities carried out by a French manufacturing corporation selling through its own sales agents or employees abroad even without a foreign permanent establishment.* 90 The benefits from the exemption could be greater in sales to a low-tax country. Secondly, when a foreign subsidiary repatriated its profits to its parent company in the form of dividend, 95 per cent of the dividend was deducted from the taxable income of the parent company and the remaining 5 per cent was considered to be deducted as ordinary expenses.* 91 This was so regardless of whether the subsidiary was subject to taxes in the country of residence, or whether the tax rate in that country was less than the French rate. Thirdly, the arm's length pricing rule was not strictly applied by the French authorities when taxpayers could prove that competition conditions in foreign markets required deviation from arm's length pricing. The relaxed inter-company pricing rule amounted to an exemption from French tax of "virtually the entire profits from the manufacture and sale of exported goods, approaching the maximum subsidy which could be implemented by any tax mechanism."* 92 Fourthly, although the territoriality principle represented a reasonable approach to avoid double taxation, the resulting effects of its application could not be excluded from being a remission or exemption of taxes, and therefore a form of export subsidy. It was the trade effects rather than the intention that should be the concern. * 93. Fifthly, despite of the fact that a French firm could not deduct foreign losses, it was permitted to deduct against domestic profits certain expenses or losses in the establishment of foreign branches.*[94]

In reply, France argued that the territoriality principle, which respected the fiscal sovereignties of states and which provided a proper mechanism to avoid double taxation through exemption, was in conformity with international fiscal doctrin prevailing in Europe and was supported by numerous international studies.*[95] Secondly, with regard to taxing on dividends repatriated from a subsidiary, one could not deem the exemption as a general form of relief as in most instances the subsidiary was subject to foreign taxation and usually there was further levy when the allocation was made.*[96] Thirdly, the departure from the arm's length principle in the case of meeting competition was not a case of subsidy as alleged by the U.S., because it was extremely likely that the same situation might develop between independent companies. A supplier might have an interest in the profitability of its marketing company.*[97] Fourthly, deduction for a start-up losses incurred abroad was intended to be a remedy for a French firm handicapped in establishing undertakings by the rule that it could not deduct foreign losses rather than an incentive for exports.*[98]

The Panel considered that the territoriality rule as practiced by France "allowed some part of export activities, belonging to an economic process originating in the country, to be outside the scope of French taxes",*[99] and thus created a pecuniary benefit to exports directed to countries having more liberal corporation tax provisions. Although the beneficial effects of the practice were incidental to the French tax system, it still constituted a partial exemption from direct taxes and a subsidy on exports. The provisions regarding dividends were a supplementary device to reserve those benefits. Meanwhile the benefits would increase as a result of any departure from the arm's length principle.*100 the Panel also gave similar verdicts to the territoriality rules as applied by Belgium and the Netherlands, which with few variations were essentially the same as that applied by French. *101

International double taxation is one of the most complicated issues in the negotiation of tax treaties. An ideal solution of double taxation should take into account several considerations, including tax sovereignty of each country, tax neutrality with regard to trade or capital flows, inter-country equity in the allocation of tax revenues, and the role of tax as a policy instrument. However, the Panel in the territoriality case only followed the criterion of trade neutrality. As far as tax neutrality is concerned, the existing methods for the elimination of double taxation adopted by tax treaty models are inadequate to achieve absolute neutrality.* 102 The exemption method as exemplified by the application of the territoriality rule is unsound because of the differences in the tax systems and tax rates among trading countries. The credit method, according to which all taxes on income paid in the source country are entitled to be deducted from the tax on the income in the resident country, is a better approach to trade neutrality. However, there are rare instances where the resident country allows a full credit to the tax paid abroad or allows refunds of that part of tax paid abroad which exceeds the amount due under the rate of resident country. Achievement of absolute neutrality requires fundamental changes in the existing international tax arrangement. For instances, a resident country would grant full credit or refund the excess only when it is assured that due compensation will be made to its revenue losses by the source country. Thus, there is a need for clearing arrangement either on a bilateral or on a multilateral basis.

The problem of neutrality and equity will be much more complicated when the two countries concerned maintain different systems with regard to the integration of personal and corporate income taxes.*103 In some cases there may even be a need for deviation from the conventional principle of non-discrimination in tax treatments.*104

Although unsatisfactory, the credit and the exemption methods are the only available means in eliminating double taxation without fundamental changes which trading countries are not prepared to accept. In so far as export sales through establishments abroad are concerned, the exemption method is able to place exporters in a more advantageous position than the credit method. When the sales activities occur in the country maintaining more liberal tax rates, the sales incomes are not subject to further taxation in the resident country of the parent company, while the credit method requires further taxation. Conversely, when the sales activities occur in a country maintaining higher tax rates, both methods do not provide compensation for higher taxes paid abroad, because the exmeption method does not allow deduction for tax paid abroad and the credit method is usually accompanied by a ceiling for the permissible level of credit. Technically, it is possible for the exemption to create a case where incomes from exports are subject to lower taxes than incomes from domestic sales and therefore to create a case of export subsidy, while under no circumstances such a case would be created under the credit method. If the adoption of the exemption method is thus condemned there will be a dilemma for a country which adopts the method because of historical reasons or other considerations and finds no feasible alternatives. For such a country, the trade effects may be incidental. Thus, an exception should be given to such a case and difference in arrangements in eliminating double taxation are to be treated as given. This means such use of exemption method should not be considered violative of the GATT obligations. Recognizing the difficulty of those countries following the exemption method in avioding double taxation, the Subsidy/Countervailing Duty Code in its notes provides that the Code does not intend to limit a signatory from taking measures to avoid the double taxation of foreign source income. In addition, the GATT Council in accepting the Panel's decision on the present case also reiterated this understanding.* 105 However, granting benefits to exporters through practices associated with the exemption method, such as less stringent application of the arm's length principle without justification, should be considered as a violative export subsidy. A country whose trade interest is affected to some extent by the use of exemption method can litigate under the non-violation nullification clause. Neverteless, there remains the problem of seeking proper remedies for such a case.

The argument by the U.S. that the DISC legislation was intended to remedy the distortion created by the application of the territoriality principle was a false one. Unilateral countervailing actions without authorization by the governing body of international trade was a technical violation of the GATT obligations. Besides, to correct a distortion by creating another distortion rather than eliminating the first distortion at its source may raise the question of whether the world as a whole is better or worse off after such a correction. When there exists a tribunal to adjudicate disputes, it is the tribunal rather than individual nations that is to decide what remedy should be given to the adversely affected party. The only exception is countervailing duties which can be used to offset the distortion without prior authorization, provided various requirements for such an action have been fulfilled. However, countervailing duties can only protect the import-competiting industries, and for its export interest, a complaining country has to take the case to the adjudicating body of the GATT. Should it successfully prove there is a case for granting remedies, the Contracting Parties would urge the parties to reach a mutually acceptable solution. Under such circumstances, it is tempting to trade off between two distortions, one caused by the complaining country and the other by the defending country. Indeed, the settlement reached between the U.S. and those European countries involved was an agreement that both parties could tax their exporters as they saw fit. Such an ending may be a happy one for the parties concerned, but it may have serious consequences. Other countries may follow suit and through tax legislations they can grant benefits to their exporters under the disguise that their actions are intended to be remedies against the European practices or even the U.S. practices. Thus, the existence of an unremovable distortion justifies many other distortions. It may be that such an arrangement can give disputing parties a broadly defined sense of justice, but it is done at th expense of global efficiency.

Finally, the U.S. asserted that, according Article 31 of the Vienna Convention, any subsequent agreement between the parties or any practice in the application could be references in interpreting a treaty.*106 The DISC legislation and the territoriality rule can be deemed as such practices. The assertion is arguable. When a treaty, like the GATT, is equipped with its own adjudicating body, it is the adjudicating body that is to interpret the treaty; or when it is equipped with a multilateral consultation mechanism, a valid interpretation should be produced through multilateral consultations rather than bilateral trade-offs.

(ii) Trade Neutrality Revisited

As noted previously, indirect taxes are not fully shifted forwards and direct taxes not fully backwards. It is probable that the full-shifting rule could lead to an inequitable situation that in a country where the market conditions make producers absorb part of the indirect taxes, the producers would receive benefits from full refunds of the indirect taxes paid when goods are exported, and thus more resources will be allocated to the production of exported goods. On the other hand, in a country where direct taxes are usually partially shifted forwards, producers would have the disadvantage of not having any refund of that part of the taxes. In the first case, other countries could still establish a case of export subsidy, if they could prove that producers in the country concerned have received more beneficial treatments in export trade than in domestic trade. This is because the rule that any refund in excess of the indirect taxes levied on domestically traded products is considered as an export subsidy does not mean that a refund less than those for domestically traded goods is not an export subsidy. In fact, the rule only provides a ceiling beyond which there is definitely a case of export subsidy, and under which it is still possible to find a case as such.*107 The analogy cannot be applied to the second case. A country accused of granting partial or full exemption of direct taxes to exports could not rebut the assumption of export subsidy on the ground that exported goods do not receive more beneficial treatments than domestically traded goods. This is because the definition of export subsidy regarding direct taxes does not draw reference to the tax treatment to domestically produced goods. It could only defend itself by asserting that the "benefits" do not cause significant trade effects as changes in the incidences of direct taxes are not presumed to be reflected in prices or sales efforts.*108 Then it is the complaining country's responsibility to prove there exists actual damage. Through the shift in burden of proof with regard to trade effects, it becomes more difficult to establish a case for compensation and therefore the inequitable situation can be eased to some extent. Nevertheless, such an approach may provide a loop-hole for a real case of export subsidy through refunds of direct taxes. The best way to solve the difficulty would be to revise the definition of export subsidy with regard to direct taxes so that export subsidies in the case of direct taxes can only be found when exported goods receive more favourable treatment than domestically consumed goods.

(iii) Taxes Occultes

Taxes occultes, or in the Code's language "prior stage indirect taxes", are dealt with in item (h) of the illustrative list. Exemption, remission or deferral of cumulative taxes occultes on goods or services used in the production of exported goods is allowed to the extent that it does not exceed exemption, remission or deferral of taxes occultes in the production of like products for domestic consumption.*109 Countries, like the U.S., still maintaining a cascade system may incorporate into their tax systems a principle which excludes from taxation products used by the purchaser for further manufacture, in order to prevent any inefficiency that may result from double taxation on the same item.* 110 Exemption of taxes occultes for exported products is in fact an extention of such a principle so that the treatments to domestically consumed and exported products can be equalized. In countries where the cascade system is adopted and there is no such an exemption principle embodied in the tax system, taxes occultes on goods for the production of exported product can be exempted, only when the goods are physically incorporated in the exported product. In the case of a non-cumulative tax, such as a VAT, the above mentioned rule does not apply and taxes occultes levied under a VAT system are to be governed by the rule regarding general definition of export subsidy discussed above. Thus, taxes occultes of this type can be fully refunded or exempted.

(iv) Drawbacks of Import Charges

Import charges are defined as tariffs, duties, and other fiscal charges not included in other kinds of taxes in the illustrative list.[*111] Remission or drawback is allowed for import charges levied on imported goods that are physically incorporated into the exported good.[*112] However, such a rule may frustrate the purpose of imposing import charges, which is to protect domestic import-competing industry, because exporters always have the incentives to use imported products rather than home market products as inputs. A more liberal rule is thus provided that home market products can also be qualified for drawback under the following conditions: (1) the home market goods used as a substitute should have the same quality and characteristics as the imported goods; (2) the quantity of the home market goods used should be equal to the imported goods; and (3) the import and the corresponding export should both occur within a reasonable time, normally two years.[*113] The second requirement that the home market goods used should be in equal proportion to the imported goods limits the scope of benefits and appears to be less liberal than its counterpart in the U.S. tax law which allows full substitution of domestic for foreign inputs. Moreover, the language "the same quality and characteristics" imposed a strict limitation that goods of different quality are not allowed for such a benefit, even though the difference is insignificant and their inter-changeability is generally recognized.

(b) Export Guarantee (Credit, Cost Escalation, Exchange Risk)

As mentioned previously, any departure from commercial rates for export credit guarantees would result in misallocation of resources. However, this rationale is not followed by the GATT subsidy rule on the export credit guarantee. The GATT rule in this regard is bound by the restriction that a practice can be considered as a subsidy only when it causes bugetary losses.* 114 Thus, it is stipulated in item (j) that an export credit guarantee program is considered as an export subsidy when its premium rates "are manifestly inadequate to cover the long-term operating costs and losses of the program".* 115 Item (d) which uses commercially available terms as the criterion in defining subsidies is not applicable to export credit guarantees, because the services or products delivered by governments which are governed by item (d) should be "for use in the production" of the exported good.* 116 An export credit guarantee program, though may affect production, does not provide services to be used in production.

Two other kinds of program,i.e. export insurance programs against inflation caused by cost escalation and against exchange risks are added to item (j) after the Tokyo Round negotiations. To what extent these two programs can be considered as export subsidies had been subject to much debate and the issue was finalized in a Panel's report adopted in 1979.* 117 The conclusion of the report had led to the incorporation of these two practices into the illustrative list. The panel held the view that in the case of export inflation insurance schemes, the criterion for the determination of the existence of an export subsidy was essentially similar to that applied in the case of an export credit guarantee,i.e. whether the scheme is self-financed. A scheme could not be considered self-financed " when the total expenditure (operating costs and losses) manifestly exceeded that total income (premiums) over such a period of time and to such an extent that the shortfall could not be covered except by significant and recurrent net capital transfer from the national budget, unless there was a sufficient basis to expect that within the foreseeable future the scheme would regain financial equilibrium."*118 The Panel also specified two cases of export subsidy resulting from an export inflation insurance scheme. When a scheme could be considered as an export subsidy, it is implied in such a case that th scheme had from its inception been inherently non-self-financing and this character could not be changed by the length of time. On the other hand, a scheme could be initially self-financing but later development had changed its character and it had become an export subsidy. The remaining question is at what point in time the scheme had started operating as an export subsidy. The key factor in such a decision is the definition of the notion of "long-term". The Panel noted that in developing an operative definition, the following factors have to be taken into account: the duration of contracts covered by the scheme, the impact of particular contracts on the financing of the scheme, the delay involved in gathering and analyzing statistical information related to their operation, and particular factors present in the scheme.*119 In judging whether a scheme had resulted in an export subsidy, the past and present financial results as well as future expectation should be taken into account. And the threshold level of a scheme, according to the theory of insurance, should not be substantially lower than the relevant expected inflation rate, unless the difference was offset by an adequate level in premium payments.*120 Payments to an exporter should be related to an actual loss caused by inflationary increase in a particular transaction, and for administrative expediency, the payment could be related to upward movement of a relevant inflation index.*121 Although the Panel focused its discusson on the export inflation insurance schemes, the conclusions reached in the report could also be aplied to the export exchage rate guarantee schemes, and to some exent to the export credit guarantee schemes.

(c) Export Credit

The test in determining the subsidy element in an export credit arrangement is still the presence of government budgetary loss. Thus, an export subsidy would be found to exist when an export credit was granted at rates below those the government actually had to pay for the funds so employed.*122 In the case that export credit was financed in foreign currency, the criterion is the rates the government would have to pay, if it borrowed in international capital markets funds of the same maturity and denominated in the same currency as the export credit.*123 Exporters can still benefit from such a rule in receiving export credit supplied by governments, because government financing is non-profit-motivated and governments are usually able to borrow at lower costs and on more favourable terms than those that individual exporters (or buyers in the case of buyer credit) would incur or can obtain when borrowing from international capital markets. In addition, the payment by a government of all or part of the costs incurred by exporters or financial institutions in obtaining credits is also considered as an export subsidy, in so far as it is used to secure a material advantage in the field of export credit terms.

An export credit practice, which is in conformity with the international undertaking participated by at least twelve original signatories of the Code, is not considered as a prohibitive export subsidy, although the practice may not be consistent with the Code. It makes no difference whether the practicing country in applying its interest rate provision is a party to the undertaking or not.*124 Thus, countries, either OECD or non-OECD member countries, may apply the rates stipulated in the OECD Consensus without regard to the subsidy element in their export credit practices.

(d) Others

> "The delivery by governments or their agencies of imported or domestic products or services for use in the production of exported goods, on terms or conditions more favourable than for delivery of like or directly competitive products or services for use in the production of goods for domestic consumption, if (in the case of products) such terms or conditions are more favourable than those commercially available on world markets to their exporters."*125
>
> "The provision by governments of direct subsidies to a firm or an industry contigent upon export performance."*126
>
> "Internal transport and freight charges on export shipments, provided or mandated by governments, on terms more favourable than for domestic shipments."*127
>
> Any other charges on the public account.*128

(6) Specific Substantive Obligation: Export Subsidies on Certain Primary Products

Export subsidies on certain primary products are not prohibited by the Code except those result in the practicing signatories "having more than an equitable share of world export trade".*129 In addition to this equitable-share rule, the Code also provides that export subsidies on certain primary products to a particular market should not result in "prices materially below those of other suppliers to the same market"*130 Certain primary products are defined as products of farm, forest or fishery, in their natural forms or having undergone "such processing as is customarily required to prepare it for marketing in substantial volume in international trade",*131 with the deletion of mineral products from the original definition given in the supplementary provisions of Article

XVI.

In assessing "an equitable share of world export trade", the Code provides several guidelines. Firstly, account should be taken of the practicing signatories' shares in trade "in the product concerned during a previous representative period, and any special factors which may have affected or may be affecting trade in such product".*132

Secondly,

> '"more than an equitable share of world export trade" shall include any case in which the effect of an export subsidy granted by a signatory is to displace the exports of another signatory bearing in mind the developments on world trade'.* 133

Thirdly,

> "with regard to new markets traditional patterns of supply of the product concerned to the world market, region or country, in which the new market is situated shall be taken into ccount in determining "equitable share of world export trade".* 134

And fourthly,

> '"a previous representative period" shall normally be the three most recent calendar years in which normal market conditions existed'.* 135

The requirement "having more than an equitable share of world export trade" does not exempt all the liabilities of the subsidizing country, if other countries failed to prove the requirement. The difference between subsidies resulting in and those not resulting in "having more than an equitable share" lies in that in the former case those adverse effects essential to the establishment of a case of nullification of benefits are presummed to exist, while in the latter case they are not. Thus, a country whose subsidization on certain primary products, though not resulting in "having more than an equitable share", will still be held liable, if the complaining country is able to establish a case of non-violation nullification of benefit, or serious prejudice to its interest, or material injury to its domestic industry.

(a) Definition of Export Subsidies on Primary Products

Export subsidies on primary products are often associated with domestic price-stabilization and price-support schemes. The former under certain conditions is not considered as a subsidy practice and the latter usually only involves subsidies other than export subsidies. In determining whether a system involves a subsidy on exports, one has to distinguish it from a domestic price-stabilization scheme and a domestic price-support scheme.

In French Assistance to Exporters of Wheat and Wheat Flour ,*[136] one of the contested issues is whether the French system concerned was a scheme purely for the stabilization of domestic prices and of returns to producers, or a system involving an export subsidy. The Panel noted that the key to such a decision was whether the export operation of the French system involved financial contributions from the Government. The French system operated as follows. The Office National Interprofessionnel Cereales (ONIC) which monopolized trade in cereals including wheat and wheat flour, would purchase at a guarantee price up to a maximum amount, or quantum. The quantum included not only quantities for anticipated domestic consumption but also a margin in excess of that for export. Quantities produced in excess of the quantum were only purchased at the price that the ONIC could obtain either by selling on world markets or at concessional prices on the domestic market. The ONIC received its revenue from three sources: (1) the surplus disposal tax levied within the quantum to cover the ONIC's losses on both domestic and exported sales; (2) repayments from traders based on the price differential for wheat delivered in excess of the quantum; and (3) budgetary appropriations to finance any deficit in ONIC's operations. With regard to exports of wheat, the ONIC made payments to cover the differential between world prices and the domestic price, since the latter was usually higher than the former. In addition to the above payment, exporters of wheat flour also received payment to make up the price differential between wheat and flour in world markets and additional expenses in milling grain with a high moisture content.

It is obvious from the above that the ONIC system is partly financed by government funds. However, the main question is to what extent or whether its export operation was financed out of government funds. The Panel recognized the difficulty to assess the share of the funds in financing exports with any precision, and it assumed all items of the expenditure were financed by the budgetary appropriation at an equal percentage.*137 The result reached on such an assumption was further strengthened in the present case by the fact that even if the export losses were primarily financed by other sources of revenue than government funds, a part of the losses still needed to be covered by the latter. Thus, the Panel concluded that the French system did involve a subsidy on exports.

(b) <u>More Than An Equitable Share of World Export Trade</u>

(i) <u>World Export Trade</u>

The notion of market segmentation is often allowed in the determination of whether the effects of a specific practice are serious enough to justify counteractions in the administration of antidumping and countervailing duties. Market segmentation means when adverse trade effects in one of the markets constituting the whole international or domestic market are serious enough, the country thus adversely affected is justified to take legitimate unilateral counteractions or to request for remedies under the multilateral dispute settlement scheme. In such a case, the remedies are limited to offset the adverse effects in the particular market concerned. Such a mechanism is also used in the observation of the competitive effects of a practice in the application of municipal competition laws. However, in the case of subsidies on primary products, the Panel in the French Assistance to Exporters of Wheat and Wheat Flour held the view that 'the concept of "equitable" share was meant to refer to share in "world" trade of a particular product and not to trade in the product in individual markets.'*138 Thus, when the adverse effects of export subsidies on certain primary products arise from the displacement of exports of other countries, the effects of displacement in the individual markets should be assessed by reference to the world market as a whole. In other words, having a more than equitable market share in an individual market will not suffice, the market share should be calculated in terms of the world market as a whole. On the other hand, the adverse effects of subsidies other than export subsidies on certain primary products can be found to exist when they arise from displacement of exports of other countries in a third country market or the domestic market of the subsidizing country. Under such circumstances, the world market can be segmented into individual markets, and adverse effects occuring in a specific individual market will be sufficient for a case of nullification of benefits, serious prejudice or material injury, if the effects are serious enough. For instance, a displacement of 50% of the market share in a third country market, for subsidies other than export subsidies on certain primary products, will be sufficient to establish a case of nullification or serious prejudice. However, if the 50% market share of that market only constitutes 1% of the word market share, it is probable that the adverse effect is not serious enough.*139

Another definitional problem of the term "world export trade" was raised in the European Communities' Refunds on Exports of Sugar case.*140 In that case, the complaining Australia argued that the term "world export trade" meant the "world free market", namely, the market "accessible to all exporters on the basis of open competition and where, in consequence, the price effects of such competition occurred".*141 It also drew analogy to the distinction made by the International Sugar Agreement between "free market" and special arrangement trade. The Panel rejected the Australian contention not because the argument was unsound but because that "a consideration of shares of the free market involved methodological difficulties that would make any comparison difficult".*142

(ii) Previous Representative Period

A very cautious process of selecting a "previous representative period" was carried out in the European Communities' Refunds on Exports on Sugar.*143 The period subject to complaint was from 1976 to the time the action was being adjudicated by the Panel, including 1976, 1977 and controversially 1978. The Panel faced three alternatives as a result of the abnormal market condition in 1974/1975 when the market prices were abnormally high. The reasons for the high prices were that 1974 was the fourth consecutive year that world total consumption exceeded world production, and the bad crop in 1974. There was therefore a shortage of sugar in the European Communities in 1974/1975, and some exports were delayed from 1975 to 1976. The Panel thus considered 1975 not sufficiently representative and had doubts on the qualification of 1974. The three alternatives the Panel had were (1) 1971-1973, the most recent calendar years for which market conditions could be considered normal, (2) 1972-1974, assuming 1974 was still qualified, and (3) 1972, 1973 and 1976, in so far as the comparison was to be made with 1977. The Panel applied all three alternatives and made a set of comparioson with the time periods, 1976-1977, 1976, and 1977, and found that the increases in market shares in all comparisons were under 2.1% and were rather small. However, when the controversial 1978 was taken into account, the result was different. The reason for 1978 being controversial was that at the time the complaint was presented to the GATT, the year 1978 had not yet ended and data available for 1978 were not finalized. 1978 is also special because in that year the International Sugar Agreement of 1977 came into force and modified certain elements of the international sugar market. Following the precedent made in the Canadian Lead/Zinc case,*144 that full statistics for the applicable base period did not have to be available at the very beginning of the negotiations or adjudicating proceedings, if the data would become available later on and be submitted without unduly delay, the Panel used the 1978 data in making the comparison and found that the increase in market shares in 1978 was significant. The Panel thus concluded that the significant increase of the Community exports justified the examination of its development.

(iii) Equitable Share

No definition of "equitable share" has ever been given. The Panel in the French Assistance to Exports of Wheat and Wheat Flour case simply concluded that the substantial increase in the market share of French exports, together with the facts that as a result of the subsidy in issue French exporters were able to quote prices for wheat lower than other exporters and that the prices quoted by French exporters for wheat flour barely exceeded those for wheat, meant that the French share of world export trade was more than equitable. *145 The Panel in the European Communities' Refunds on Exports of Sugar went a step further and conducted a more detailed analysis of the term "more than an equitable share" by looking into the reasons for developments in individual market shares, and by examining market and price developments. The Panel first found that the increase in French exports was significant and continued to seek whether the increase in world market shares was resulted from displacing Australian exports. Displacement according to the Panel's finding did not occur in four of the five groups of markets constituting the world markets, where either the Community or Australia was the main supplier. Only in one market in the remaining group, where the Community and Australia were competing with each other, Australian exports fell while the Community's exports increased considerably. However, supplies from other countries to that market also increased considerably at the same time. The Panel thus concluded that there was not sufficient evidence to prove the increased Community exports considerably directly displaced Australian exports from world markets. In so far as indirect displacement was concerned, the Panel noted that under certain circumstances, raw sugar which was Australia's predominant sugar export could be replaced by white sugar. Although the Panel found that Community's exports of white sugar had expanded in some traditional raw sugar markets, it was deterred from concluding that the Community exports had indirectly resulted in some displacement of Australia's exports. This was because the increased Community 's exports might be the result of re-export of raw sugar imported from developing countries under special arrangements.* 146 The Panel also drew attention to the facts that a substantial share of the Australian exports was under long-term arrangements, and the operation of the ISA in 1978 resulted in certain contraction of exports of its members. Therefore the Panel found that it was difficult to establish a causal relationship between the increase in the Community's exports resulted from the subsidy practice concerned and the fall of the Australian exports. It is worth noting that in the present case, the Panel implicitly considered that a case of "more than an equitable share" should comprise three elements: significant increase in world market caused by a subsidy, considerable market displacement, and a causal link between the two.

Another problem with regard to "more than an equitable share", although unresolved, was raised in the United States Subsidy on Unmanufactured Tobacco.*147 The case was handled through a consultation conducted by a working party, rather than by an adjudicating panel. In that case, the U.S. alleged that the U.S. export subsidies on unmanufactured tobacco were intended to prevent the continuing erosion of its relative position in the world market and to regain its equitable share of world trade. The secular decline in the United States share was due to (1) the increased competitiveness of the developing countries, partly enhanced by the preferential arrangements in some markets, (2) a change in manufacturers' requirements in the importing countries, and (3) most importantly, the U.S. domestic price support policies together with domestic legislations prohibiting differentiation of prices for export and domestic sales. The complaining Malawi contended that the concept of equitability did not refer to the maintenance of a predetermined proportinate share of a growing world market. Some members of the Working Party emphasized that the pattern of supply to world markets could not be regarded as static and should allow for changes in relative competitive position, especially when the spirit of the GATT was taken into account. Bypassing the U.S. argument of remedying the disadvantage resulting from domestic price policies, Malawi concentrated on the issue of increased competitiveness of the developing countries. It argued that according to Article XXXVI:3,*148 the share of the less developed countries in world trade in a particular commodity could grow at a faster rate than world trade as a whole, and the rate of export growth by the industrialized countries. This arguments was supported by Canada which maintained that the preferential arrangements regarding exports from developing countries should be deemed as an element of international competition rather than a distortion to be corrected. Since the case was not vigorously pursued by Malawi, and was only dealt with in a consultation, there was no opportunity to establish a panel to rule on two important issues in the determination of "more than an equitable share": (1) whether market shares lost because of domestic price policies can be regained for the purpose of maintaining an "equitable" share; (2) whether more weight should be given to the developing countries in calculating the market shares. In regard to the second point, the Code provides that trade and development needs of developing countries should be taken into account in assessing market displacement.*149 The position of Malawi in the present case is thus confirmed.

(iv) <u>Causal Relationship between Export Subsidy Practices and Increased Exports</u>

The remaining work in setting up a case of "resulting in the subsidizing country having more than an equitable share of world export trade" is to seek whether and to what extent the increase of exports can be attributed to the export subsidies in question. The process of reaching such a decision was exemplified in the case of <u>European Communities' Refunds on Exports of Sugar</u>. *150 Under the EEC sugar system, the intervention agencies of the Community would buy sugar within a maximum product quota at a guarantee price, and sugar produced in excess of the basic quota but still within the maximum quota was subject to a levy of up to 30% of the intervention price. Export refunds were made to the total of maximum production quota, plus imports under the

Lome Convention and the Cane-Sugar Agreement, minus domestic cunsumption, in order to prevent domestic pricing from being affected by price fluctuations in the external market. The refund was intended to compensate the difference between the prices prevailing outside and inside the Community. The Panel found that the continued growth in production stimulated by the price policy, together with a downward shift in consumption in 1975 significantly increased exportable surpluses of sugar. The Community's quota system and the levy device were unable to prevent surpluses from increasing, because, though the plant areas were reduced, total production continued to increase as yields were higher. Thirdly, the Panel found the amount of refund was not subject to budgetary limitation as the exportable surpluses increased. Fourthly, the Panel also found that the increase in the Community's sugar exports mainly consisted of increased export with export refunds, i.e. sugar produced within the maximum quota. Thus, the facts that the pricing policy stimulated the increase in surpluses, that the Community system failed to control production, and that the increased export with refunds constituted the main elements of the increase in exports, led to the conclusion that the increase in the Community's exports could be attributed to the operation of the Community's regulations. The conclusion was not explicitly mentioned in the Panel's conciliation report, where the Panel's discussion appeared to be confusing.* [151] In the section concerned, the Panel started with the question of a causal relationship, but after discussing each element as mentioned above in the Community system it turned to the conclusion that there was no element in the system that could prevent the Community from having more than an equitable share of world export trade in sugar. The conclusion then led to the verdict that the system and its appliction constituted a threat of prejudice to the interest of Australia. One may therefore assume that the Panel in reaching such a verdict had in mind that the incrase in exports could be attributed to the operation of the system. It is still unclear though what the intensity of a causal relationship is needed in linking up an export subsidy practice and the increase in exports.

(c) Price-Undercutting

Export subsidies on certain primary products which result in prices materially below those of other suppliers to the same market are also prohibited by the Code.* 152 The existence of such a subsidy is presumed to result in adverse effects necessary to demonstrate nullification or impairment of benefits under the GATT.

(7) Specific Substantive Obligation: Subsidies Other Than Export Subsidies

The Code recognizes the importance of subsidies other than export subsidies as an instrument for the promotion of social and economic policies, and therefore it does not restrict signatories' rights in such pursuits. It specified some of the objectives of this nature as follows:* 153

> "(a) the elimination of industrial, economic, and social disadvantages of specific regions,
> (b) to facilitate the restructuring, under socially acceptable conditions, of certain sectors, especially where this has become necessary by reason of changes in trade and economic policies, including international agreements resulting in lower barriers to trade,
> (c) generally to sustain employment and to encourage re-training and change in employment,
> (d) to encourage reserach and development programmes, especially in the field of high-technology industries,
> (e) the implementation of economic programmes and policies to promote the economic and social development of developing countries,
> (f) redeployment of industry in order to avoid congestion and environmental problem."

The Code also gives examples of possible forms of such subsidies. They are: *154

> "government financing of commercial enterprises, including grants, loans or guarantees, government provision or government financed provision of utility, supply distribution and other operational or support services or facilities; government financing of research and development programmes; fiscal incentives; and government subscription to, or provision of, equity capital."

It is recognized that the use of such subsidies may cause or threaten to cause adverse effect,i.e. material injury to a domestic industry of another signatory, serious prejudice to the interest of another signatory, or nullification or impairment of benefits. Thus, in drawing up their policies and practices, signatories are required to take into account possible effects, in addition to the evaluation of internal objectives to be achieved.*155 Signatories should also seek to avoid causing adverse effects.*156

The Code's approach to subsidies other than export subsidies as mentioned above is unclear. Unlike in the case of export subsidies, it does not prohibit the use of subsidies other than export subsidies in pursuing national objectives, except those causing adverse effects to the interest of other signatories. This straight-forward rule fails to clarify the following issues. Firstly, whether the Code assumes all subsidies other than export subsidies are linked to specific policy objectives, and whether it is possible to find such subsidies which is not aimed at a specific policy objective except to strengthen the competitiveness of the domestic producers. This is unclear because the Code only mentions that subsidies other than export subsidies are widely used in the pursuit of policy objectives and does not say what its attitude towards non-policy objective-linked subsidies is, if there exists such a subsidy in the drafters' minds. A related problem is what the case will be when the magnitude of the subsidy in question exceeds that needed to achieve a specific policy. Secondly, whether there is a distinction between more justified and less justified objectives. If the answer is positive, are those enumerated in the Code more justified? And in the case that a specific objective is not enumerated in the Code, the practicing country should prove its compatibility with those enumerated. If negative, what is the effect of such enumeration? One can imagine two possible interpretations of such enumeration. (1) The enumeration may impose the presumption of legitimacy in using subsidies to achieve such objectives and the practicing country is relieved from the burden of proving the justifiability of a specific objective. The interpretation is preconditioned by the assumption that there is a distinction between more justified and less justified objectives. (2) The enumeration can be interpreted as removing any illegitimacy in using subsidies as a policy instrument. This interpretation is also subject to two preconditions, that there is a distinction of justifiability and that there is a presumption of illegitimacy on using subsidies other than export subsidies regardless of whether they are aimed at specific objectives.

The answer to the above questions may simply be that the Code treats all aubsidies other than export subsidies equally and the only thing that matters is the trade effects of such subsidies. The enumeration of objectives has no implication at all and does not by itself create any basis for action under the General Agreement.*157 If a complaining country intends to initiate the dispute settlement proceeding, it shall demonstrate the existence of sufficient adverse effects as a procedural requirement. This is because the existence of subsidies other than export subsidies alone is not sufficient to constitute a cause of action, unlike in the case of export subsidies where adverse effects required to demonstrate nullification or impairment of benefits are presumed to exist when there is a failure to comply with the GATT rules regarding export subsidies. Nevertheless, in so far as countervailing duties are concerned, it makes no difference whether the subsidy in issue is an export subsidy or not, because the assumption of existence of adverse effects does not apply in the determination of material injury. Submission of evidence with regard to the existence of injury is required in all circumstances.

(8) Specific Substantive Obligation: Developing Countries

In addition to the special consideration given to developing countries in assessing adverse effects arising from market displacement, the Code also provides special rules regarding the use of subsidies by developing coutries in Part III of the Code. Just as the Code's rules on dispute settlement are derived from Article XXII and Article XXIII of the General Agreement, Part III is an application of Article XVIII, which allows developing countries to deviate temporarily from provisions of the General Agreement, and Part IV of the General Agreement, which stipulates that preferential treatment should be accorded to developing countries.*158

The Code first recognizes that "subsidies are an integral part of economic development programmes of developing countries", and does not "prevent developing country signatories from adopting measures and policies to assist their industries, including those in the export sector".*159 In the case of export subsidies, the Code provides the following special rules for developing countries. Firstly, the rule that "signatories shall not grant export subsidies on products other than primary products" does not apply to the developing countries, unless otherwise provided. Instead, the developing countries only agree that subsidies on their <u>industrial products</u> should not be used in a manner which causes <u>serious prejudice</u> to the trade and production of another signatory.*[160] Thus, with regard to subsidies on certain primary products, developing countries are still under the obligation that subsidies should not be used in a manner which result in their "having more than an equitable share of world exprt trade" or results in material price-undercutting.*[161] Secondly, the mere use of an export subsidy by developing countries is not violative, and there is no presumption that it causes adverse effects in so far as nullification or impairment is concerned. The adverse effects should be demonstrated by positive evidence,"through an economic examination of the impact on trade or production of another signatory".*[162] Thirdly, even if an export subsidy granted by a developing country results in serious prejudice, or nullification of benefits, the Committee on Subsidies and Countermeasures should not authorize countermeasures to other signatories.*[163] This is conditional on (1) that the developing country concerned had entered "a commitment to reduce or eliminate export subsidies when the use of such subsidies is inconsistent with its competitive and development needs"; and (2) that the subsidy in question is in accordance with the terms of the commitment. Such a commitment also relieves a developing country from the Committee's review of its export subsidy practices for the period of commitment.*[164] Developing countries, however, are not fully safeguarded by the above mentioned devices. Export subsidies by developing countries, though within the terms of a commitment, are still subject to the most effective countermeasures,i.e. countervailing duties, if they cause material injury to the domestic industry of an importing country.

Differentiation of treatment is also made for subsidies other than export subsidies. With respect to such subsidies, actions, including the request for consultation, the request for conciliation, the request for review of the subsidies in question, and countermeasures may not be taken or authorized.* 165 However, there are two exceptions:(1) when the subsidy causes nullification or impairment of tariff concessions or other obligations under the General Agreement in such a way as to displace or impede imports of like products into the market of the subsidizing country;* 166 and (2) when the subsidy causes material injury to the domestic industry of an importing country.* 167 The second exception means that countervailing duties can still be employed to offset the adverse effects of a subsidy other than export subsidies used by developing countries. In any event, third country markets are still open for the developing countries to compete, with competitiveness enhanced by subsidies other than export subsidies and without entering into commitment as required in the case of export subsidies.

The Code also makes distinction between government intervention and subsidies other than export subsidies used by developing countries. It, recognizing that "in developing countries, governments may play a large role in promoting economic growth and development", provides that " intervention by such governments in their economies, for example through the practices enumerated in paragraph 3 of Article 11, shall not, per se , be considered subsidies."*168 It is unclear what criterion shall apply in making such a distinction. One might infer from the Code's language and define government intervention aimed at promotion of economic growth and development as not per ser subsidies. The importance of making such a distinction lies in that government interventions when not considered as subsidies are not subject to the restrictions imposed by the Code, including countervailing duties and authorized countermeasures in certain circumstances, whereas subsidies other than export subsidies, in the case of the developing countries, are still subject to the above mentioned two exceptions. In application, governments of the developing countries can always resort to the economic development rule by claiming the government action in question is aimed at promoting economic development. Other signatories have no way to challenge the claim under the Code, unless the government action causes nullification or impairment of tariff concessions or other obligations under the GATT in such a way as to impede or displace imports to the subsidizing country, or material injury to the domestic industry of an importing country. Under these two circumstances, other signatories can request for consultation on government intervention concerned by treating it as an ordinary subsidy other than export subsidies. Through the dispute settlement proceeding thus initiated, the specific government action can be examined.

(9) Specific Substantive Obligation: State Controlled Economies

So far we have based the discussion of subsidy on the assumption that the structures of the economies under examination are market economies, i.e. prices as well as allocation of resources are determined by market forces. Subsidies are considered as another determinant, in addition to market forces, created by government action, or to be more precise, government fiscal contribution. Government action in this context is an abnormal economic phenomenon, and the major function of subsidy law is to remove or to prevent such abnormality from disturbing the free operation of market forces. However, in an economy where government action is the predominant factor in directing allocation of resources, government intervention should be considered as a normal phenomenon. Since every economic activity in such an economy is under the influence of government action, it would make no sense to seek whether or to what extent a product exported therefrom is benefited from a subsidy. Rather, the main concern in dealing with such exports is to prevent them from disturbing the operation of markets outside that economy, by bringing the prices of such exports in line with those prices determined by market forces. An importing country can thus be allowed to levy antidumping or countervailng duties or to use other countermeasures to offset the differences between the prices of such exports and the prices that the exporters would charge if the product concerned was produced in a market economy.

Article 15 of the Code provides that in the case of alleged injury caused by imports from "a country which has a complete or substantially complete monopoly of its trade and where all domestic prices are fixed by the State",*169 the importing country may base its procedures and measures on the Code or the International Antidumping Code. The calculation of the margin of dumping or of the amount of estimated subsidy can be made by comparing the export price either with the price at which a like product of a country other than importing signatory is sold or with the constructed value of a like product in a country other than the importing signatory. Constructed value means cost of production plus a reasonable amount for administration, selling and any other costs and for profits.*170 When the price or the constructed value so established cannot provide an adequate basis for comparison, the price in the signatory countries, if duly adjusted to reflect reasonable profits, may be used.*171 Furthermore, the calculation should be based on prices and costs ruling at the same level of trade, normally at the ex-factory level, and made as nearly as possible at the same time.*172 Due allowance should be made for any differences affecting price comparability.*173 The issues of comparison and of determination of price and cost to be compared with will be discussed in detail in the section dealing with antidumping duties.

(10) Dispute Settlement: Consultation, Conciliation, Adjudication and Authorization of Countermeasures

(a) General

The Code provides a set of procedural rules for the signatories to settle their differences regarding the use of subsidies. The procedure starts with consultation between two disputant signatories. If the consultation fails to clarify the facts of the situation and to arrive at a mutually acceptable solution, the dispute can be referred to the Committee on Subsidies and Countermeasures for conciliation.*174 Should the conciliation fail, the Committee shall, upon request , review the matter usually through a panel. *175 After the review, the Committee should make recommendation as may be appropriate to resolve the dispute.*176 Finally, when the recommendations are not followed, the Committee may authorize countermeasures, taking into account the degree and nature of the adverse effects found to exist.*177

The procedural rules for dispute settlement, like the substantive rules, also make differentiation of treatment on export subsidies and subsidies other than export subsidies. Because of the presumption of the existence of adverse effects for demonstrating nullification and impairment, a signatory which believes that an export subsidy granted by another signatory is inconsistent with the Code may request consultation with the latter signatory.*178 Nevertheless, conditions for a signatory to request consultations regarding any subsidy are that it believes the subsidy is granted by another country and that it also believes the subsidy causes injury to its domestic industry, nullification or impairment of its benefits, or serious prejudice to its interest.*179 Consequently, the request for consultation, in the case of export subsidy, should include a statement of evidence with regard to the existence and nature of the subsidy in question;*180 while in the case of any subsidy, there should be evidence not only with regard to the existence and nature of the subsidy in question, but also with regard to the injury caused to the domestic industry; or in the case of nullificaion or impairment or serious prejudice, the adverse effects caused to the signatory requesting consultations.*181 Moreover, when consultation on a subsidy fails to reach a solution within thirty days the issue may be referred to the Committee for conciliation; while in the case of any subsidy, the time period allowed for consultation is sixty days.*182 Both time limits, however, can be extended by a mutual agreement between the disputing parties.*183

(b) Committee on Subsidies and Countermeasures

The Committee on Subsidies and Countervailing Measures is established to perform several functions: (1) to provide opportunities of consultation for signatories on any matter relating to the operation of the Code or the furtherance of its objectives,*184 (2) to conciliate disputes among signatories,*185 (3) to authorize countermeasures in the event that its recommendations regarding a dispute are not followed,*186 (4) upon request, to review export subsidies granted or maintained by the developing countries,*187 (5) to review annually the implementation and operation of the Code, and to inform the Contracting Parties of the development,*188 and (6) to monitor the administration of countervailing duties by the signatories.*189

The Committee is composed of representatives from each of the signatories and may set up subsidiary bodies, such as a panel or a working party , as necessary.*190

(c) Panel

The Committee, upon the request of either of the parties in dispute, is to establish a panel to review the facts of the case, and basing on the findings regarding the facts, to investigate the rights and obligations of the disputing signatories as interpreted and applied by the Code.*191 The Panel should be established within thirty days after the request, and its finding should be delivered within sixty days after its establishment.*192 The panel is composed of three or five members and the composition should be agreed by both parties.*193 Preference is given to governmental members, and citizens of the disputing countries are understood not to be the panel's members.*194 Panel members would serve in their individual capacities and not as government representatives, and should be so selected as to ensure the independence of the members, a sufficiently diverse background and a wide spectrum of experience.*195

(d) Mutually Satisfactory Solutions

The Code encouages parties in dispute to develop mutually satifactory solutions and provides several opportunities throughout the dispute settlement proceedings for the disputants to reach such a solution before the Committee makes its recommedations and authorizes countermeasures. At the initial stage of the dispute, the parties are allowed thirty or sixty days to settle their differences through consultations.*196 In the following period of conciliation, the Committee acts as a conciliator providing its good offices for both parties. The third opportunity comes when the panel has finished its investigation and submits its report including its conclusions to the parties in dispute and before the report is sent to the Committee.*197 Being thus informed of the panel's decision and bearing in mind the possible recommendations the Committee will make, the disputants may then be more flexible in negotiating mutually acceptable solutions.

(e) Scope of the Committee's Jurisdiction

The GATT dispute settlement procedures have long been criticized as ineffective, partly because of lacking substantive rules as the foundation for its operation. The Tokyo Round negotiations of the GATT produced several codes of conducts in an attempt to develop substantive laws in areas where such developments are possible. It is expected that these substantive foundations together with the incorporation of the general model of dispute settlement stipulated in Article XXII and Article XXIII into each code would set the stage for general reform of the dispute settlement procedure in the future.*198 The power of the Contracting Parties is distributed to the individual committees established to be in charge of the administration of the codes. There is however the problem of jurisdictional conflicts. As far as the Subsidy/Countervailing Duties Code is concerned, it is natural to take a case of nullification or impairment of benefits accruing to the complainant under the Code to the Committee on Subsidies and Countermeasures. It is also conceivable that a subsidy practice can nullify or impair the benefits under other codes, and the benefits of the Subsidy/Countervailing Duties Code can be nullified or impaired by measures outside the Code's scope. The Code's position seems that nullification or impairment of any benefit accruing to contracting parties under the General Agreement by a subsidy can be litigated under the Code's dispute settlement scheme, no matter whether the subsidy is in violation of the Code. When benefits under the Code have been nullified by a measure outside the Code,the proceeding should be initiated, according to the nature of the measure concerned, under other codes or Article XXIII of the General Agreement. Such a conclusion is derived from the requirement that in requesting for consultation and initiating the dispute settlement procedure under the Code, the complaining country should, among others, demonstrate the existence of a subsidy. The Code's approach towards definition of jurisdiction is different from those of other codes, most of which define their jurisdiction by using such language as "any party considers that any benefits accuring to it, directly or indirectly, under this Agreement is being nullified or impaired, or that the attainment of any objective of this Agreement is being impeded...",(emphasis added)*199 or "trade interest in civil aircraft manufacture, repair, ... have been or are likely to be adversely affected....".*200 Thus, if a benefit resulting from other countries' compliance with the Antidumping Code is nullified by a subsidy, both the Committee on Subsidy and Countermeasures and the Committee on Antidumping Practices will all have the jurisdiction over the issue. Moreover, when a benefit under the Agreement on Trade in Civil Aircraft which eliminates customs duties and other charges with regard to trade in civil aircraft is nullified by the use of a subsidy, the issue will fall within the jurisdiction of both the Committee on Trade in Civil Aircraft and the Committee on Subsidies and Countermeasures.

The second issue in connection with the jurisdiction of each committee is its relationship with the Contracting Parties, i.e. whether the Contracting Parties can overrule the decisions of each committee. This problem is not mentioned in the documents produced during the Tokyo Round negotiations. Even if the committees' decisions are final, there is still a need for a supervising body to handle the jurisdictional conflicts among the committees. Moreover, since not all contracting parties of the General Agreement are signatories of the codes, disputes between non-signatories are still to be settled before the Contracting Parties and there still remains the problem of disputes between non-signatories and signatories.

Finally, the dispute settlement procedures provided in the Subsidy/Countervailing Duty Code are available not only to disputes arising from the use of subsidies but also to those from the misuse of countervailing duties. Throughout the investigation, the administrating authority is required to afford reasonable opportunities for consultations to the signatory whose exported products are under investigation. Such consultations may establish the basis for proceeding under the Code's settlement scheme.*201

(f) Further Discussion on Dispute settlement

Traditional institutional dispute settlement can be in three forms: (1) judicial proceedings, (2) arbitration, and (3) conciliation and mediation. One of the differences between them is the legal force behind them. Conciliation and mediation carry no legal binding force on both parties in dispute, while arbitration and judicial proceedings do. Court decisions have direct binding effect on both sides of the dispute, whereas arbitral awards, though theoretically binding, need court action to enforce, when one of the parties fails to comply. Court actions intended to implement arbitral awards are based on the contractual obligation of the party that disputes between them should be referred to an arbitration body. Another difference betwen settling disputes in a court and in an arbitration body is that the former is mandatory except in those areas where disputants are allowed greater autonomy, such as commercial transactions or labour disputes. Arbitration is however based on the contractual relation between parties. This means the parties can decide whether their dispute shall be referred to an arbitration.

The GATT dispute settlement mechanism is a combination of conciliation and arbitration. It is not of judicial characters, because the GATT is an organization structured on a multilateral contract rather than a supra-national body equipped with the faciliaties of and functioning as a government at the international level. GATT's jurisdiction over the disputes between the contracting parties is derived from the contractual obligation of each party. It is mandatory in the sense that when entering into the General Agreement, contracting parties agreed that future disputes should be settled according to the rules and procedures stipulated in the Agreement. Thus, whenever a dispute occurs, the GATT has the automatice jurisdiction over the dispute without further consent by the parties in dispute. The whole dispute settlement procedures prior to the authorization of counteractions is more of a conciliation than arbitration process. This is because before the authorization, the GATT functions as a conciliator, and parties can settle their disputes by mutually agreed solutions. This is so even after the investigating panel has reached its decision on the issue in dispute, which prior to authorization is not binding on both parties. The authorization of counteraction adds the characteristics of an arbitartion to the dispute settlement mechanism, i.e. it gives binding force to the decisions of the Contracting Parties.

Arbitral awards in the present case are not to be enforced by national courts as they concern state-to-state public contractual relations, and well beyond the jurisdiction of national courts. The enforcement of the arbitral awards is rather rested on the economic power of a contracting party that can be exerted on the other contracting party in the dispute. This enforcement issue, together with the enforcement of GATT rules, is discussed further in the following section.

(g) Enforcement Mechanism

In discussing international agreements, there is always the problem of their enforceability. Unlike municiple laws, international agreements have no effective means to sanction violation. This is so even in some cases where an international agreement is equipped with a supra-national framework for its implementation. The GATT is of no exception. The flow of goods among trading nations means the economic interest of a country would be to some extent affected by another country's action. Thus, a country can be "sanctioned" by being denied market access or equal treatment to its exports. Such sanction which involves restricting trade flows from a particular source is ironically in conflict with the underlying rationale of the GATT,i.e. free trade. A means of sanction whose frequent use may frustrate the purpose of the agreement can hardly be an effective one. Moreover, the effectiveness is also conditional on the economic power of the country which is in the position to impose sanction against another country. If the former country imports little from the latter country or the latter does not require imports from the former, the latter country shall have no reason to be deterred by the imposition of sanction by the former country. Collective sanction by all other countries than the country violating the rules can be effective, but it's feasibility is very much in doubt as it is difficult to expect countries to impose sanction which would hurt their own short-term interest only to protect the interest of the country immediately vitimized by the violation.

As sanction by individual or collective counteraction may fail to serve effectively the purpose of implementing an agreement aimed at trade liberalization, a less formal but more effective mechanism has emerged under the GATT system. The main characteristic of the mechanism is the gradual accumulation of international pressure on the country taking or intending to take an action which may have the effect of nullifying the benefits accruing to other countries under the GATT. The operation of the mechanism starts with the obligation of consultation with the country likely to be adversely affected by an action not consistent with the GATT rules. In the process of consultation, the acting country would face the first pressure from the country it consults with. If this first pressure fails to persuade the acting country to terminate its action, the pressure would increase when a competent organ of the GATT, such as the Committee on Antidumping Practices, intervenes in the dispute as a conciliator. The pressure from the Committee will be stronger after a panel has investigated the dispute and reached a verdict not in favor of the acting country. The panel's finding presumably reflects the international consensus on the issue in dispute and points the direction of international opinion which in turn exerts pressure on the acting country. Another mechanism for the formation of international pressure is the meetings of each committee. In such meetings, each country can express its opinion on a specific practice of a contracting party and through the exchange of views international opinion can be formed.

An important step for the formation of international opinion is to bring the violation to international attention, i.e. to bring the issue to the proper machinery of the GATT. Coercision or bribery may prevent a violation to be brought to international attention. A system of surveillance and prosecution can remedy such a deficiency. All the committees of the GATT are equipped with a surveillance system, but only the Textiles Committee is empowered to review all restrictions on textile trade through the Textile Surveillance Body which would submit its findings to teh Textile Committee without specific initiatives from participating countries. The findings will therefore be discussed in the meetings of the Committee. The findings will also be taken into account by the Contracting Parties which has the power to impose sanction, when a complaint on the same issue is brough to it. The significance of such kind of prosecution system largely lies in its effect on the formation of a ruling according to which a formal sanction can be imposed. This is because imposition of sanction under the GATT system is still subject to the condition that there shall be a dispute and the dispute is referred to the GATT by the parties in dispute.

Conclusion

1. Non-Distortive Subsidies

As discussion in Chapter I, some subsidies are used to correct existing distortions and some may not cause distortions. Both subsidies, though not distortive, may result in effects on the competitive relations between the producers in the practicing country and those in other countries. If the sole purpose of the Code is to reduce or to eliminate distortion in trade and production, there is certainly no need to interfere with the use of non-distortive subsidies. However, the Code never makes a clear distinction between distortion and adverse effects on the existing trade interest of another country. It is stated in the preamble of the Code that signatories desire "to ensure that the use of subsidies does not adversely affect or prejudice the interest of any signatory...". Throughout articles of the Code, the emphasis is on whether a subsidy has caused adverse effects on the interest of other signatories. There is no specific rule for non-distortive subsidies to be exempted from any liability, although in the preamble it is also stated that the MTN should "reduce or eliminate the trade restricting or distorting effects on non-tariff measures...", including subsidies. It may be that the Code assumes that subsidies that restrict trade are always distortive. Such assumption does not take into account the fact that non-distortive subsidies may also affect the interest of another country. The lack of direct ptotection of non-distortive subsidies makes a signatory, in defending its subsidy practice, have to resort to the nullification or impairment clause for protection. This would involve enormous burdern in demonstrating the benefit claimed to be nullified and the trade effects of an anti-subsidy measure. Protection of non-distortive subsidies under the nullification or impairment clause is in fact a cautious approach. This is because there are no clear definitions as to what constitute external economies, and as to what extent a subsidy intended to remove existing distortions can be considered as not excessive. Moreover, real cases of non-distortive subsidies are extremely rare. Many distortive subsidies are used under the disguise of efficiency-enhancing objectives, and it is also difficult to resist the temptation to extend a subsidy beyond the extent necessary to achieve an efficiency improving objective. The difficulty in establishing a case of non-violation nullification would deter to some extent the abuse of the argument of non-distortive subsidies.

2. Export Subsidies

(a) Dual Pricing : The confusion as to whether dual pricing is still a prerequisite for the use of counteractions shall be clarified. It is quite possible that it is still required for holding a country liable for its export subsidy practice. However, the importance of such a requirement has become insignificant, because of the interpretation made in the Report on Export Insurance Scheme that all export subsidies are presumed to ensue dual pricing.

(b) Presumption of Adverse Effect : The presumption of adverse effects imposed on the use of export subsidy under the Code is more confined than the presumption of nullification or impairment under Article XXIII. This would render the nullification or impairment clause under the Code useless as a complaining party can more easily establish a case of nullification and impairment under Article XXIII.

(c) Tax-Shifting Assumption : The adoption of the complete shifting assumption may lead to an inequitable situation as taxes are not actually completely shifted forwards or backwards. In the case of indirect taxes, the inequity can be remedied by establishing a case of non-violation nullification when the amount of refund or exemption is lower than the upper limit stipulated in the Illustrative List. In the case of direct taxes, the inequity can be eased to some extent by the changes in the burdern of proof of the necessary trade effects. A better approach is to define export subsidy in this regard by reference to tax shifting conditions in domestic trade.

(d) Export Guarantee, Export Insurance, and Export Credit : The definition of export subsidy in this regard should give more weight to commercial terms in order to prevent exporters from benefiting from the difference between commercial terms and terms based on the cost consideration.

3. Developing Countries

The special treatment accorded to developing countries shall be extended to the use of countervailing duties. Meanwhile, the definition of developing country shall be clarified, especially when those newly industrialized countries are concerned. This so-called "graduation issue" should be dealt with through coopration with other international economic institutions, such as the IMF, the World Bank or the UNCTAD.

4. Jurisdiction of the Committee

Different approaches used by the Codes in defining scopes of concern result in the problem of jurisdictional conflicts. Moreover, it is also unclear as to the relation of the Contracting Parties to each Committee.

Footnotes (Part Two, Chapter II)

1. GATT BISD Vol. IV, pp. 26-7
2. Ibid
3. Ibid, pp. 68-9
4. BISD 26S/56-83

5. Review Pursuant to Article XVI:5, Report by the Panel adopted on 24 May 1960, (L/ 1160), BISD 9S/188, 189-191

6. Operation of the Provisions of Article XVI, Report adopted on 21 November 1961 (L/442 & Add. 1-2) BISD 10S/201, 208

7. Note 1, Article 7 of the Code, BISD 26S/ 56, 67
8. Section 771 (/) U.S. Trade Agreement Act , 19 C.F. R. 335.7 (a) 1980 45 Fed. Reg. et. seq.

9. Note 4 accompanying Article 19:4, BISD 26S/56, 76
10. Note 2 accompanying Article 19:4, BISD 26S/56, 78
11. Review pursuant to Article XVI:5 (1960), see note 5 , p. 191
12. Ibid, pp. 191
13. see the discussion of export insurance scheme below

14. Article III:8 (b) BISD Vol. IV p.7
15. Italian Discrimination against Imported Agricultural Machinary, Report Adopted on 23 October 1958, (L/833), BISD 7S/60. The Panel in this case ruled that credit facilities granted to the purchasers of agricultural machinary could not be considered as subsidies accorded to the producers of the agricultural machinery concerned. pp.64

16. Note 2 accompanying Article 1 of the Code, BISD 26S/56, 57
17. Article III:1, BISD Vol. IV, pp.6
18. Review Pursuant to Article XVI:5, Para. 10, p. 191, see note 5
19. Ibid
20. Ibid

21. i.e. use of subsidy shall not cause injury to the domestic industry of an importing country.

22. Article 8 of the Code, BISD 26S/56, 67-8

23. Note 1 accompanying Article 8:3 and note 4 accompanying Article 2:1, BISD 26S/56, 68, 57

24. Uruguayan Recourse to Article XXIII, Report Adopted on 16 November 1962 (L/1923), BISD 11S/95, 99-100. The Panel's ruling in this case were incorporated into the Understanding Regarding Notification, Consultation, Dispute Settlement and Surveillance (adopted on 28 November 1979 (L/497) BISD 26S/ 210) as para. 5 of its Annex --- Agreed Description of the Customary Practices of the GATT in the Field of Dispute Settlement (Article XXIII:2)

25. The Australian Subsidy on Ammonium Sulphate , Report Adopted by the Contracting Parties on 3 April 1950, (GATT/CP.4/39) BISD Vol.II, 188
26. Ibid, p.193
27. BISD 3S/224
28. R.E. Hudec, " Retaliation against "Unreasonable" Foreign Trade Practices: the New Section 301 and GATT Nullification and Impairment ", Minnesota Law Review Vol.59, p. 461
29. Treatment by Germany of Imports of Sardines , Report Adopted by the Contracting Parties on 31 Oct.1952 (G/26) BISD 1S/53. This case was very similar to the Australia Subsidy case. The case involved German import duties on two kinds of sardin which were biologically distinct but commercially competitive and were imported respectively from Potugal and Norway. Germany was imposing more restrictive import control on Norwegian imports. In 1951, Norway had obtained tariff concessions on its sardin products from Germany. Norwegian negotiators had also asked for an assurance that future imports of Norwegian sardin would not be treated less favourablly than the imports from Portugal. The assurance was given, though not in writing. Therafter, German Government found itself bound by its domestic law and failed to carry out the assurance. The case was then brought to the GATT for adjudication.

30. German Import Duties on Starch and Potato Flour , 3S/77, Report Adopted by the Contracting Parties in 1954. In the 1950-1 tariff negotiations, a letter was delivered by the German delegation to the Benelux delegation. The letter stated that (1) the German delegation agreed that German duties on certain starch products "should be reduced as soon as possible to the level of duties applied by the Benelux" and (2) the German Government would open negotiations in these regards with the Benelux governments as soon as possible. Negotiations did take place, but without success. The German Government later notified the Benelux governments that tariff reductions could not be implemented in the resonably near future, because of certain German price-support programmes. The Benelux governments then asked the GATT to investigate the case and to make a recommendation.
31. see note 21
32. see note 29
33. see note 30
34. EEC--- Programme of Minimum Import Prices, Licences and Surety Deposits for Certain Processed Fruits and Vegetables, Report of the Panel Adopted on 18 Oct. 1978 (L/4687) BISD 25S/68,93

35. Grandfather clause allows national legislations pre-existing the General Agreement to preempt the provisions of the General Agreement.
36. Nullification of the benefits of equity is by its natre a kind of non-violation nullification, because it involves no voilation of the obligations under the GATT.
37. Uruguay Recourse to Article XXIII , Report Adopted on 16 Nov. 1962, (L/1923) BISD 11S/95
38. Ibid, para.21-22, pp.101-2
39. Ibid, para. 15, pp. 99-100
40. Ibid, para. 22, p.102
41. For a discussion of the legislative history of Article XXIII, see Hudec, note 24
42. Part IV of the General Agreement, BISD Vol.IV, pp.53
43. A case of similar nature can be seen in the United States Subsidy on Unmanufactured Tobacco , (Report of the Working Party on Article XXII:2

Consultation Adopted on 22 Nov. 1967 (L/2925) BISD 15S/116. In this case, the U.S. claimed that its subsidy on tabacco products was justified because it was intended in part to offset the preferential treatment that the developing country, including the complainant Malawi, enjoyed in markets where the U.S. products had to compete with those of these countries. Since tobacco was within the category of primary product, one of the central issues was the determination of an "equitable share". Malawi, basing on Part IV of the General Agreement, argued that the share of the less developed countries in world trade in a particular commodity could grow at a faster rate than world trade as a whole, and the rate of export growth by industrialized countries. Thus, the secular decline of the U.S. share in world trade should be deemed as normal development rather than a distortion in world trade. The view was supported by Canada which argued that the preferential treatment that the developing countries enjoyed should be recognized as an element of international trade, asnd should not be expected to be offset by subsidies. Since the case was discussed under a working party in the form of consultation, and was not vigorously pursued by Malawi, it was not able to be adjudicated by a panel in order to establish a test case in regard to the benefit of equity.

44. i.e. rates of duty in one country's tariff scheduale differ more widely than did those in the tariff scheduales of other countries, although the differences in tariff levels might be relatively small.

45. see note 112

46. European Communties--- Refunds on Exports of Sugar , Report of the Panel Adopted on 6 Nov. 1979 (L/4833) BISD 26S/290, 319. As to the trade effect of the EEC practice, see the discussion in the following section.

47. see note 112

48. French Assistance to Exports of Wheat and Wheat Flour , Report Adopted on 21 Nov. 1958, BISD 7S/46

49. see note 15

50. see note 117

51. Ibid, para. 3.33-3.51

52. Ibid, para. 3.78-3.83

53. see note 46

54. see notes accompanying Article 8:4 of the Code, BISD 26S/56, 68

55. Article 8:4 of the Code, BISD 26S/56, 68

56. see discussions in the following section regarding the use of export subsidy

57. note 7 accompanying Article 9 of the Code

58. note 4 accompanying Article 9 of the Code

59. Article 9 of the Code

60. United States Tax Legislation (DISC), Report of the Panel presented to the Councile of Representatives on 12 Nov. 1976 (L/4422) BISD 24S/134, para. 72; Income Tax Practices Maintained by France , Report of the Panel presented to the Council of Representatives on 12 Nov. 1976 (L/4423), BISD 24S/114, para.51; Income Tax Practices Maintained by Belgium , Report of the Panel presented to the Council of Representatives on 12 Nov. 1976 (L/4424) BISD 24S/127, para 38; Income Tax Practices Maintained by the Netherlands , Report of the Panel presented to the Council of Representatives on Nov.1976 (L/4425), BISD 24S/137

61. Article XVI:4 of the General Agreement, BISD Vol. 4, p.27

62. Export Inflation Insurance Schemes , Report of the Panel Adopted on 25 July 1979 (L/4813) BISD 26S/330, para. 12

63. U.S. Executive Branch GATT Study, No. 2, 'GATT Provisions on Unfair Trade Practices', pp. 4-6

64. Ibid

65. Item (e) of the Illustrative List of Export Subsidies, Annex of the Code
66. Item (f) of the Illustrative List
67. Item (g) of the Illustrative List
68. Note 1 of the Illustrative List
69. Ibid
70. Ibid
71. Ibid
72. see note 143
73. the DISC, see note 143, para. 1-22
74. Ibid, para 28
75. Ibid. para 30
76. Ibid, para 37
77. Ibid, para 31
78. Ibid, para 33, 34
79. Ibid, para 35
80. Ibid, para 38
81. Ibid, para 72
82. Ibid, para 75
83. Ibid, para 39-42
84. Ibid, para 79
85. Ibid, para 47
86. Ibid
87. Ibid, para 79
88. Ibid, para 73
89. see note 143
90. Ibid, para. 3-16
91. Ibid, para 30
92. Ibid, para 26
93. Ibid, para 32
94. Ibid, para 35
95. Ibid, para 20
96. Ibid, para 31
97. Ibid, para 27
98. Ibid, para 36
99. Ibid, para 47
100. Ibid, para 49-54
101. see note 60
102. The OECD Model Double Taxation Convention on Income and Capital adopts both the exemption and credit methods as alternatives for elimination of double taxation. (Article 23A & B) The U.S. Model Treaty (1977 Tax Treaties (P-H) II 1019) only adopts the credit method. (Article 23) For discussions of the exemption and the credit methods, see R.J. Patrick, Jr., " A Comparison of the United States and OECD Model Income Tax Convention ", 10 Law and Policy in Int'l Bus. pp. 613, 695-701; The United Nations Group of Experts in preparing guidelines for tax treaties between developed and developing countries also adopted both methods as alternatives, but in comparing with the limited use of the credit method it considered the exemption method as more useful in encouraging investment in developing countries. see Surrey, "United Nations Group of Experts and the Guidelines for Tax Treaties between Developed and Developing Countries", Law and Policy in Int'l Bus. Vol.10:2, pp.1, 43-7
103. For a detailed discussion in this regard, see Mitsui Sato, "International Aspects of Integration of the Corporation and Personal Income Taxes", Ga.Int'l 779
104. see Iames G. O'Brian, " The Non-discrimination Article in Tax Treaties

", Law and Policy in Int'l Bus. Vol.10:2, p.545
105. Tax Legislations, (L/5271), BISD 28S/114
106. see note 60, the DISC, para 42
107. only without the assumption of the existence of adverse feffects
108. The Panel in the DISC and the territoriality cases, when discussing the trade effects of exemption of internal corporate income tax, indicated that there was a presumption that an export subsidy would lead to any or a combination of the following consequences in the export sector: (1) lowering of prices, (2) increase of sale effort, and (3) increase of profit per unit. The Panel however did not discuss the presumption which formed the basis of the GATT rules regarding the definition of export subsidy in the case of border tax adjustment, that indirect taxes are shifted forwards completely. The presumption was used by the U.S. delegation in defending the U.S. practice.
109. Item (h) of the Illustrative List of Export Subsidies, BISD 26S/26, 81
110. Internal Revenue Code of 1954, as amended and in force on Jan. 3, 1961, Chapter 65, Section 6416
111. see note 1 of the Illustrative List
112. Item (i) of the Illustrative List, BISD 26S/56, 81
113. Ibid
114. see the text accompanying note 12 & 13
115. The Illustrative List, BISD 26S/56, 81
116. Ibid, p.80
117. Export Inflation Insurance Scheme , Report of the Panel Adopted on 25 July 1979 (L/4813) BISD 26S/330
118. Ibid, para 15
119. Ibid, para 17
120. Ibid, para 9
121. Ibid, para 11
122. Item (k) of the Illustrative List, BISD 26S/56, 81
123. Ibid
124. Ibid
125. Item (d) of the Illustrative List, BISD 26S/56, 80
126. Ibid, Item (a)
127. Ibid, item (c)
128. Ibid, Item (l)
129. Article 10:1 of the Code, BISD 26S/56, 69
130. Article 10:3 of the Code
131. Note 7 accompanying Article 9 of the Code
132. Article 10:1
133. Article 10:2(a)
134. Article 10:2(b)
135. Article 10:2(c)
136. see note 48
137. Ibid, para 13
138. Ibid, para 15, see also European Communities---Refunds on Exports of Sugar , see note 129, para 4.9
139. Such a differentiation of treatment to subsidies on primary products from treatment to non-primary products is not explicitly provided in the Code, In note 6 accompanying Article 8:4(c) which provides that the adverse effects of a subsidy can arise from a displacement of exports of another signatory from a third country market, it is stipulated that " the problem of third country markets so far as certain primary products are concerned is dealt with exclusively under Article 19 below ". In Article 10, there is no reference to third country markets, and instead, the notion of world export trade is used in dealing with market displacement. World export trade is

interpreted as the world market as a whole. This, together with the fact that the phrase ' " more than an equitable share of world export trade" includes any case of displacement of exports of another signatory ' is not followed by such language as " from a third country market " , leads to the conclusion as illustrated in the text. In other words, adverse effects which are necessary to establish a case of nullification or impairment or serious prejudice arising from market displacement should be assessed by reference to the world market as a whole. This conclusion however does not apply to adverse effects of other events such as price undercutting.

140. see note 46
141. Ibid, para 2.20
142. Ibid, para 4.9
143. see note 46
144. <u>Canada--- Withdrawal of Tariff Concessions</u> , Report of the Panel on Lead and Zinc Adopted on 17 May 1978 (L/4636) BISD 26S/42, 48
145. see note 48, BISD 7S/46, para 15-9
146. see note 46, BISD 26S/290, para 4.29-4.34
147. see note 43
148. Article XXXVI:3 stipulates that "there is need for positive efforts designed to ensure that less-developed parties secure a share in the growth in international trade commensurate with the needs of their economic development" BISD Vol.IV, 54
149. Note 5 accompanying Article 8:4(c) of the Code
150. see note 46
151. Ibid, para 4.29-4.35
152. Article 10:3
153. Article 11:1
154. Article 11:3
155. Article 11:2
156. Ibid
157. Article 11:4
158. Article XVIII, BISD Vol.IV, pp.28-30, Part IV of the General Agreement, Vol.IV, pp.53
159. Article 14:1 & 2
160. Article 14:3
161. Article 10
162. Article 14:4
163. Article 14:6
164. Article 14:8
165. Article 14:7
166. Ibid
167. The Countervailing Duty Code does not provide special treatment to the developing countries.

168. Article 14:7
169. Annex 1, Article VI:1 point 2, BISD Vol.IV,pp.64
170. Note 1 accompanying Article 15
171. Article 15:3
172. Article XVI:4
173. Ibid
174. Article 17:1
175. Article 17:3

176. Article 18:9
177. Ibid
178. Article 12:1
179. Article 12:3
180. Article 12:2
181. Article 12:4
182. Article 13:1, 2
183. Note 1 accompanying Article 12:1
184. Article 17:1
185. Article 18
186. Ibid
187. Article 14:8
188. Article 16:1
189. Article 2:16
190. Article 16
191. Article 18:1
192. Article 18:2
193. Article 18:3
194. Article 18:4
195. Article 18:5
196. Article 13:1
197. Article 18:6, 7
198. R. E. Hudec, ' Adjudication of International Trade Dispute ', p. 45
199. Article 15:2, Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade (International Antidumping Code) BISD 26S/171
200. Article 8:7, Agreement on Trade in Civil Aircraft, BISD 26S/162
201. Note 1 accompanying Article 3:2 of the Subsidy/ Countervailing Duty Code

PART TWO

Chapter III

Countervailing Duties under the GATT

Chapter III .: Countervailing Duties under the GATTT

(A) Introduction to pre-1979 Countervailing Duty Law under the GATT

The remedy provided for an adversely affected importing country by a subsidy in Article XVI, i.e. bilateral consultations between disputants and authorized withdrawal of concessions, usually requires a long period of negotiation and bargaining, and therefore may not provide a swift remedy. Countervailing Duties provided in Article XVI allow the government of an importing country to take relatively speedier and unilateral actions to offset the effect of a subsidy.*1 The use of countervailing duties is subject to the condition that the subsidy involved causes or threatens to cause materal injury to an established domestic industry, or retards materially its establishment. An importing country can also impose countervailing duties on a subsidized import which causes material injury to the domestic industry of another country. Dual pricing as a result of the operation of a system for the stabilization of the domestic prices or incomes of domestic producers of an primary product should not be considered to cause material injury. Moreover, when an export subsidy enables an exporters to practice dual pricing, only countervailing duties or antidumping duties can be used to offset the effects of the practice.

(B) Countervailing Duties after the Tokyo Round

A countervailing duty, as defined in the Code, is "a special duty levied for the purpose of offseting any bounty or subsidy bestowed directly or indirectly upon the manufacture, production or export of any merchandise..."*2 Countervailing duties are provided as an alternative remedy for an importing country whose domestic industry is injured by subsidized imports. The provisions on subsidies and dispute settlement, and on countervailing duties can be invoked in parallel. But with regard to the effect of a specific subsidy in the domestic market of an importing country, only either countervailing duties or authorized countermeasures can be used. *3 Countervailing duties are a self-defense instrument that can be used by individual countries without authorization from the GATT, and their administration is governed by domestic law. However, if the imposition of countervailing duty is not subject to international discipline at all, a country may turn this defensive instrument into an offensive one . Thus, Article VI and the Code stipulate those international obligations that countries should comply with in their legislation regarding countervailing duties. The purpose of Article VI and the Code is to provide both substantive and procedural safeguards to countries whose exports are under investigation by the administrating authority of an importing country. The procedural rules are as important as, if not more important than, the substantive rules, because the investigating procedure rather than countervailing duties themselves may also cause damage to the trade interest of the exporting country. This is because once the procedure is initiated, it adds uncertainty to commerical transactions and business secret is in danger of being publicized.

(1) Substantive Rules

There are three substantive requirements for the imposition of countervailing duties: the existence of a subsidy, injury to a domestic industry, and a causal link between the subsidized imports and the alleged injury. The determination of the first requirement has been discussed in the last chapter and the latter two are discussed in the following.

(a) Injury to Domestic Industry

(i) Injury

The term "injury" means " material injury to a domestic industry, threat of material injury to a domestic industry or material retardation of the establishment of such an industry ..." (emphasis added)* 4 Determinations of injury should be based on positive evidence, whereas in the determination of threat of injury, the evidence of the nature of the subsidy in question and the trade effects likely to arise therefrom may be taken into account.* 5 The determination process should contain two objective examinations: (1) the volume of subsidized imports, and their effect on prices in the domestic market for like products, and (2) the subsequent impact of these imports on domestic prices of like products.* 6 In examining the volume of subsidized imports, the investigating authority should consider whether there has been a significant increase in subsidized imports, either in absolute terms or relative to production or consumption in the importing country. In regard to the effect of the subsidized imports, there shall be investigation into their price effect, including whethere there has been a significant price-undercutting or whether they have the effect of depressing prices to a significant degree or preventing price increases.* 7 These factors are to be considered collectively, and no one or several of them can necessarily give decisive guidance.* 8

The Code also gives a list of factors to be considered in the examination of the impact on the domestic industry. The list is not exhaustive, nor can one or several of the listed factors be necessarily decisive. These factors are: (1) all relevant economic factors and indices having a bearing on the state of the industry such as actual or potential decline in output, sales, market share, profits, productivity, return on investments, or utilization of capacity; (2) factors affecting domestic prices; (3) actual or potential negative effects on cash flow, inventories, employment, wages, growth, ability to raise capital or investment; and (4) in the case of agriculture, whether there has been an increased burden on government support programmes.* 9

These indicia of injury are ordinary indicia of business injury rather than indicia of competitive effects. This is because countervailing duties are aimed at protecting domestic producers rather than domestic consumers.

The guidance as listed in the Code is qualitative in nature, and the Code does not give quantitative guidance in the determination of injury except the interpretative note saying that injury means "material injury". The word "material" does not suggest much and its substance is subject to signatories' interpretations. A Group of Experts in a 1959 report stated that "Antidumping measures should only be applied when material injury, i.e. substantial injury is caused or threatens to be caused" (emphasis added).*10 That material injury is a synonym of substantial injury is not mentioned in the Code and this would probably be the intention of the signatories to leave the term "material injury" as vague as possible. The U.S. is the only signatory which incorporates a definition into its domestic countervailing duty legislation. Prior to the enactment of the U.S. Trade Act of 1974, the U.S. International Trade Commission (formerly Tariff Commission) in dealing with antidumping duties from the case Cast Iron Soil Pipe from Poland *11 onwards discarded its previous practice which considered injury must be material and there should be an anticompetitive effect. Instead, the Commission adopted the principle that injury of more than de minimis degree would be sufficient for the imposition of antidumping duties. In the legislative history of the Trade Act of 1974, the Senate Finance Committe held the view that "injury must be a harm which is more than frivolous, inconsequential, insignificant, or immaterial"*12 but no specific content of the injury standard was provided in the Act. There was however no clear and consistent distinction found between the test of "more than de minimis " and of "more than frivolous, inconsequential, insignificant, or immaterial" by examining post-1974 cases. The Trade Agreement Act of 1979, which is the implementing legislation of the international agreements reached in the Tokyo Round negotiations and for the first time incorporates an injury test into the countervailing duty law, defines material injury as "harm which is not inconsequential, immaterial or unimportant".*13 The House Ways and Means Committee expressively rejected the de minimis test in its report on the Trade Agreements Act, but it is repeatedly emphasized in the Senate debate that material injury in countervailing duty proceeding should be interpreted in the same manner as in the antidumping duty proceeding since the enactment of the Trade Act of 1974.* 14 Thus, the present injury test in the U.S. countervailing duty law is not much different from the de minimis test, if there exists any difference. The gain of other countries from the incorporation of an injury test into the U.S. countervailing duty legislation is therefore minimal. In fact, the gain could be negative, if one takes into account the fact that although without an injury test, the U.S. Treasury in its pre-TAA practices would not give a positive determination on the existence of a subsidy when it found the subsidy did not result in significant adverse effects on international trade.

(ii) Threat of Injury

The Code does not provide rules regarding the determination of threat of injury. However, it is provided in Article 36 of the Antidumping Code that " a determination of threat of injury shall be based on facts and not merely on allegation, conjecture or remote possibility. The change in circumstances which would create a situation in which the dumping would cause injury must be clearly foreseen and imminent ." (empahsis added)* 15 The rule is necessarily strict, as a soft standard would grossly enlarge the scope of antidumping actions. In actual practice, factors like a foreign producers's ability and willingness to dump, expansion of production capacity by foreign producers, and increases in dumped imports are often considered as indicia of threat. It is very likely that the Committee on Subsidies and Countermeasures would follow the International Antidumping Code and interpret the term "threat of injury" in the same way.

(iii) Definition of Industry

The Like Product

The term "domestic industry" is interpreted "as referring to the domestic producers as a whole of the like products or to those of whom whose collective output of the products constitutes a major proportion of the total domestic production of those products". The key in this definition is the notion of "like product" which means, as provided in the Code, "a product which is identical, i.e. alike in all respects to the product under consideration or in the absence of such a product which although not alike in all respects, has characteristics closely resembling those of the product under consideration."* 16 The term "like products" which has been subject to much controversy in previous practices is used in the General Agreement in contrast to the term "directly competitive and substitutable products"* 17 The definition given in the Code is intended to avoid any controversy that may otherwise occur, but the application of the definition as quoted above is limited to issues covered by the Code. That the like products should be products alike in all respects is an extremely narrow approach of definition and thus greatly increases the possibility of reaching a positive determination of injury. The stringency of this interpretation is furthered by the rule that in the absence of a product alike in all respects, a product having the characteristics and closely resembling the product under consideration can also qualify as a like product.* 18 This supplementary rule enlarges the scope for the application of countervailing duty law, by creating an industry which does not exist under the rule of "alike in all respects".

Identification of the Like Products

When the available data do not permit seperate identification of the domestic production of the like product in terms of such criteria as: the production process, the producers' realization, profits, the injurious effects of a subsidy should be assessed in relation to the production of the narrowest group or range of products, which includes the like products, and for which the necessary information is available.*19 The requirement that the production line to be examined should be the narrowest is to minimize the unnecessary enlargement of the industry.

Free Market

The notion of free market, which has been discussed previously in the section concerning export subsidies on certain primary products, is also a concern in the determination of domestic industry. The Code does not provide rules in this regard and the EEC Commission has used this notion extensively in determining the impact of dumping of semi-petrochemical products by the U.S. producers. The Commission noted that a part of the production of these products in the Community was consumed captively by the producers themselves and assesed the changes in the distribution of market shares by reference to the free, i.e. non-captive, market.* 20

National and Regional Markets

Although as a general rule, the domestic industry is to be composed of domestic producers as a whole, or of those of them whose outputs represent a major proportion of the total domestic production,*21 the Code allows segmentation of a nation's territory into several competitive markets and the producers within each market may be regarded as a seperate industry. To qualify as an isolated market, there are two requirements: (1) "the producers within such market sell all or almost all of their production of the product in question in that market", and

(2) "the demand in that market is not to any substantial degrees supplied by producers of that product in question located in elsewhere in the territory".* 22 Regional market segmentation is particularly useful for such industry as cement which is characterized by its high transportation costs and low value products. By employing the notion of regional industry, injury may be found to exist even though a major proportion of national industry is not injured. The determination of injury to a regional industry is further subject to two conditions: (1) there shall be a concentration of subsidized imports into such an isolated market, and that (2) the subsidized imports are causing injury to producers of all or almost all of the production within such market.* 23 The strictness of the requirements is necessary to avoid abuse of the regional market rule under which industry becomes smaller and injury may be more likely found to exist if there is no restriction on their use. The difficulty to qualify as a regional industry and to find injury to it may make the complaining domestic concern return to seeking injury to the national industry with the help of less stringent stsndard of injury. An example could be seen in the U.S. case <u>Bars and Shapes from Australia</u> where the U.S. Tariff Commission developed a principle that "an injury to a part of the national industry is an injury to the whole market"* 24 The principle can be interpreted as an application of the <u>de minimis</u> injury test of injury to the national industry and be used as a convenient device to circumvent the burden of fulfilling the four requirements for the establishment of a regional industry. Another consequence of this approach is that in the case of regional industry, countervailing duties can only be imposed on subsidized imports destined for consumption in the region concerned, whereas in th case of national industry, with a loose injury test countervailing duties can be applied

to all subsidized imports. Finally, if the constitutional law of the importing country does not permit levying countervailing duties on a regional basis,* 25 the importing country can levy countervailing duties on a nationwide basis, i.e. it can levy the duties on subsidized imports no matter whether they are destined for consumption in the region concerned.* 26 There are however two condtions for this exception: (1) the exporters have been offered an opportunity to cease exporting at the subsidized price, or to give assurance to eliminate or limit the subsidy or its effect, or to revise the prices so as to eliminate the injurious effect, but failed to do so promptly; and (2) countervailing duties cannot be levied only on products of specific producers who supply the region concerned. *27

(iv) Trade between Related Parties

When domestic producers are related to the exporters or importers or are themselves importers of the subsidized product, such producers may be excluded from the definition of domestic industry.* 28 The reason for such exclusion may be that the domestic producers have themselves contributed to the injury caused by imports, or that it is unfair for the related producers to profit from subsidized sales on the one hand and to prevent injured domestic producers from relief by enlarging the scope of domestic industry on the other hand. An important issue is the definition of the word "related" which contracting parties failed to reach in the Tokyo Round negotiations. If the reason for exclusion is that a domestic producer should be held responsible for its related concerns, the nature of the relationship needed for exclusion will depend upon whether the producer can be held responsible for the action of the related concerns. Apparent cases are the relationship between a principal and its agent, and the relationship with a branch office, but not so much in the relationship between a parent and its subsidiary. When the dividing line is whether the domestic producer can benefit from the activities of its related concern directly and indirectly, a subsidiary which repatriates its profits in the form of dividend to its parent will fall within the definition of related parties. This is so no matter whether the subsidiary actually profits from the production, importation, or exportation of the subsidized goods.

A 1981 report by a Joint Group of Experts established by the Committee on Antidumping Practices and the Committee on Subsidies and Countermeasures proposed the following definition of "related parties".

> "... producers shall be deemed to be related to the exporters or importers only if:
> (a) one of them directly or indirectly control the other; or
> (b) both of them are directly or indirectly controlled by a third person; or
> (c) together they directly or indirectly control a third person; provided that there are grounds for believing or suspecting that the effect of the relationship is such as to cause the producer concerned to behave differently from non-related producers."* 29

The term "control" means legally or operationally in a position to exercise restraint or direction.* 30 Thus, the criterion used is not the relation of profit-sharing or responsibility-sharing but the relation of control.

Another issue in regard to related parties is whether the word "industry" includes the shareholders of domestic companies only or also includes the employees of domestic companies. When the issue is put into the context of related parties, it seems that the shareholders are the sole component of the domestic industry. However, the Code lists the negative effect on employment and wages as two of the indicia of injury to be considered in the determination injury.*31 One may thus argue that the Code also considers employees as one of the components of industry. This position is consistent with that of the U.S. Tariff Commission's ruling on the case Potassium Chloride from Canada, France, and West Germany ,*32 where the Commission held that the U.S. Antidumping Act was designed to protect the interest of the domestic employees as well as the interest of the domestic corporate shareholders. One way to solve this definitional difficulty is that an administrating authority in considering whether to exclude a related producer should take into account of the employment effect. If the effect is considerable, it does not have to exclude the related producer, as the Code only says that it "may" rather than "shall" make such an exclusion.*33

(v) Industry in the case of Economic Integration

In the case that two or more countries have formed a customs union or other kinds of economic integration that has the characteristics of a single and unified market, the industry in the entire area of integration should be taken as the domestic industry for the purpose of countervailing duty.*34 However, one can expect frequent use of the notion of market segementation under such circumstances, because economic integration only removes internal tariff barriers, and there are still other factors like transportation costs, historical consumption patterns that would prevent the full integration of a national market with others.

(b) Causation

The Code requires that the subsidized imports subject to countervailing duties should be "through the effects of the subsidy, causing injury...".*35 Moreover, "... the injuries caused by other factors must not be attributed to the subsdized imports."*36 Such factors may include, among others,the volume and prices of the non-subsidized imports of the product in question, contraction in demand or changes in the pattern of consumption, trade restrictive practices of, and competition between, the foreign and domestic producers, developments in technology and the export performance and productivity of the domestic industry.* 37

The requirement on the degree of the causal link between the subsidized imports and the injury caused as stipulated in the Code and in the International Antidumping Code of 1979 is different from that under the International Antidumping Code of 1967, in which it was required that the dumped imports should be the principal cause of the injury. The term "principal cause" has been variously interpreted to mean that the injury caused by dumping should "exceed those of other factors all together",* 38 that a cause which is "greater than any other substantial or significant cause",* 39, that if the aggregate effect of all injurious factors is material injury, dumping is the principal causal factor,* 40 or dumping is individually the cause of material injury and the injury is greater than injury caused by other factors.* 41 The U.S. Tariff Commission in Ferrite Cores from Japan * 42 laid down the rule that where "more than de minimis " part of the injury was caused by the dumped imports, an affirmative determination would be rendered, regardless of the existence of other contributory factors to the injury. Furthermore, in Elemental Sulfur from Mexico , it was stated that "... all that is required for an affirmative determination of injury is that the less than fair value sales be a cause of injury to the industry, and the causation must be identifiable."* 43 Such a ruling was made possible by the fact that the U.S. in its antidumping legislation did not add the modifying word "principal" in stipulating the causation requirement. The Canadians, though also did not add the word "prncipal" into its antidumping legislation, take quite a different view. They think the word "principal" is redundant, because the proper approach towards the causation test should be that the administrating authorities must have satisfied themselves that an injury is caused by the dumped imports rather than by some other factors and then whether the injury is material.

As a result of the American and Canadian effort, though differently motivated, the principal causation test is removed from the 1979 Antidumping Code and Subsidy/Countervailing Duty Code. Nontheless, ambiguity remains. The U.S. interprets the new causation test in such a way that the subsidized imports need only be <u>a</u> cause of the injury, namely, <u>a</u> contributing factor in causing or threatening injury. The U.S. ITC in its report on the Tokyo Round negotiations emphasizes that the requirement that the dumped or subsidized imports should be <u>the only</u> cause of the material injury would render an injury test inoperable.*44 It also cites the ITC's previous practices including those of the Tariff Commission with the intention to interpret the new test in the same way. The Canadians will conceivably follow its own interpretation that the subsidized or dumped imports should be the only cause of an injury which is material. The EEC Commission, which after the Tokyo Round negotiations began to produce more detailed information regarding its administration of antidumping and countervailing duties, adopts a similar approach. The Commission in its determination of injury would first examine the effect of the imports in question in terms of the increase in the volume of imports, the increase in the market share, price undercutting, or the fall of prices in the Community's market; secondly, the loss of market share or other injuries suffered by the Community's producers; and thirdly, whether other fctors "individually or in combination" also affect the Community's industry.* 45 Finally, the Commission would conclude the injury examination by stating that the effect of the subsidized or dumped imports must, "taken in isolation", be considered as material, or vice versa .

Among those other factors the effects of which should not be attributed to the subsidzed or dumped imports, the specification of contraction of demand is an important consideration in time of recession. Trade restrictive practices of foreign and domestic producers include price-discrimination practices of domestic producers in domestic markets, infringement of trade marks, patent and trade secret, false advertising, and other unfair trade practices; competition between foreign and domestic producers may include the situations where a domestic producer in competing with foreign producers tries to monopolize the domestic market and causes injury to other domestic producers, where a domestic producer conspires with foreign producers with the intention to reduce domestic competition and thus causes injury to other domestic producers, or where the domestic producers injured simply because it cannot withstand competition from foreign imports even though there is no dumping or subsidization involved. Changes in the pattern of consumption, and development in technology and export performance and productivity of domestic industry reflect important factors that cause changes in the marketplace under current economic circumstances.

(2) Procedural Rules

(a) General Procedure

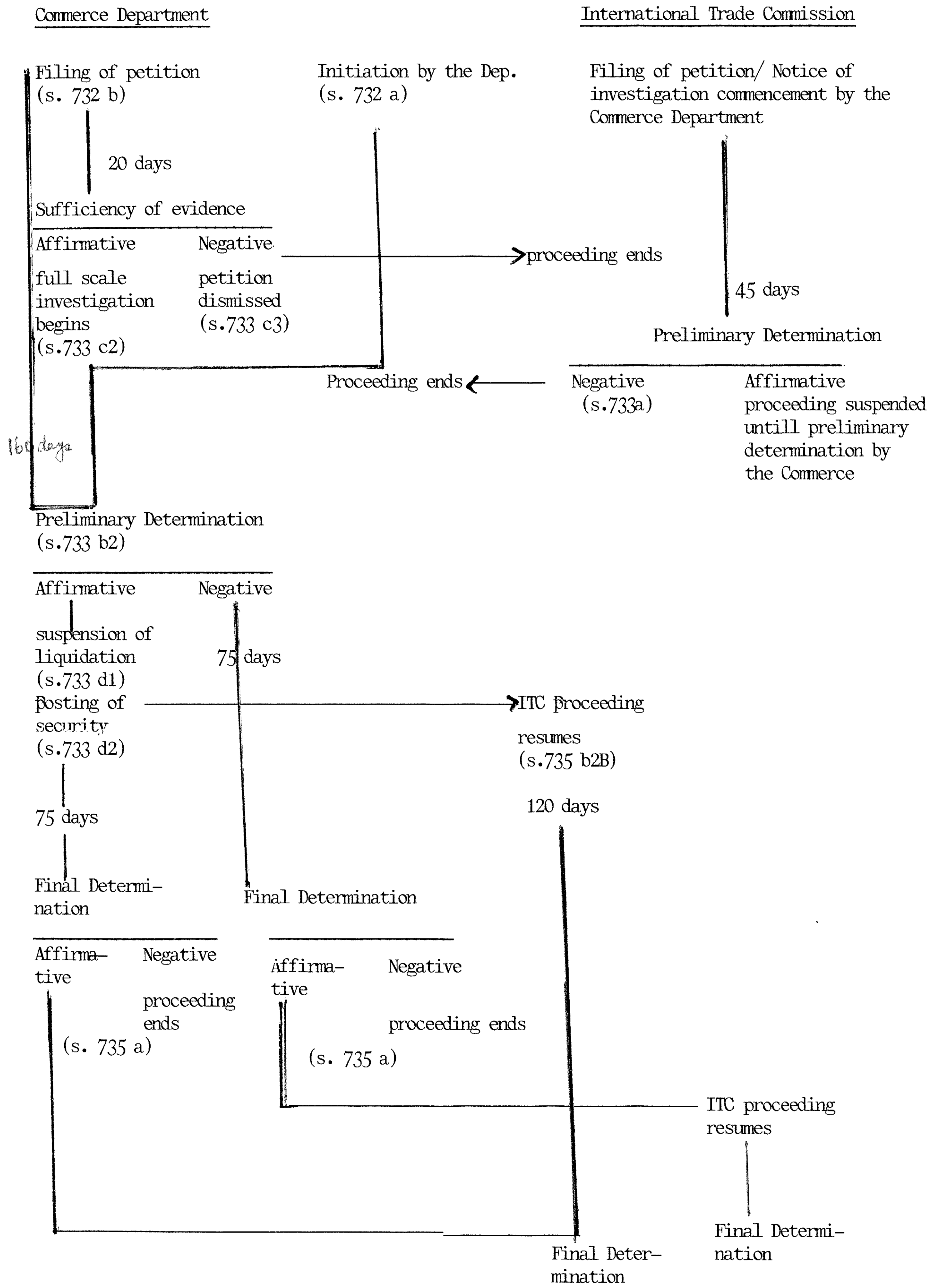
Once an antidumping or countervailing duty investigation is initiated, the importer concerned will be in a state of uncertainty. He is unable to determine the price at which the imported merchandises shall be sold, since it is unceratin when the liquidation of entries will be suspended or how much the amount of duty will be. The longer the investigation lasts, the greater the loss will be ensued. The Code therefore provides several procedural safeguards including silmultaneous consideration of subsidy and injury, time limits for the duration of investigation, public participation and access to information developed in proceedings, and protection of confidential information. Before the discussion of these safeguards, a brief introduction of the procedure that administrating authorities usually follow is necessary.

An investigating proceeding, according to the Code, shall normally be initiated upon a request or on behalf of the industry affected.* 46 The request must be in writing and includes sufficient evidence of the existence of a subsidy and, if possible, its amount, material injury and a causal link.* 47 The proceeding can also be initiated in special circumstances by the authorities concerned, if they have sufficient evidence on those three issues.* 48 Trade unions can initiate a proceeding by arguing that they are within the expanded definition of industry,* 49 or that the Code by using the word "normally" does not preclude them from filing complaints. When the authorities are satisfied that there is sufficient evidence to justify initiation, they can proceed with a full-scale investigation.* 50 The proceeding is usually divided into two broad stages. The first stage ends with preliminary decisions as to whether there exists a subsidy and whether there is sufficient evidence of injury. Should the determination be affirmative, under certain conditions, provisional measures can be applied.* 51 Provisional measures may be, as provided in the Code, in the form of provisional countervailing duties guaranteed by cash deposits or bonds equal to the amount of the proivionally calculated amount of subsidy. One provisional measure provided in the U.S. contervailing duty law is suspension of liquidation. Countervailing duties will be imposed after the final determination that there exists a subsidy and its effect has caused injury , and an assessment of the actual amount of duty.* 52 If either the determination of injury or that of subsidy is negative, the proceeding shall be terminated.

(b) Simultaneity and Time Limits

The Code requires that the evidence of both subsidy and injury be considered simultaneously in two stages of the proceeding. They are the making of the decision of whether or not to initiate an investigation, and the course of the investigation starting on a date not later than the earliest date on which according to the Code provisional measures may be applied.* 53 In other stages of the proceeding, the Code also encourages stimultaneous consideration. * 54 The whole investigating proceeding shall be concluded within one year after its initiation.* 55 The requirement of simultaneity is relatively easy to meet for those countries where the investigation is conducted by a single authority. For countries like the U.S. where the investigation is seperately conducted by two government agencies, one dealing with the determination of injury and the other the determination of subsidy, strict simultaneity is difficult to maintain. To economize and to avoid unnecessary waste of resources, such seperate administrations usually follow the procedure that one authority decides whether there exists a subsidy; and upon an affirmative determination of a subsidy, the other authority will begin its investigation on injury. To accomodate such administration, the Code does not require that simultaneity be maintained throughout the investigation. The U.S. countervailing duty procedure modified after the Tokyo Round in order to conform with the Code's requirement is demonstrated in the chart on the next page. The modified procedure requires simultaneous filing of petition to both the Commerce Department and the U.S. International Trade Commission which is the counterpart of the ~~Federal~~ Trade Commssion in the field of international

The U.S. Antidumping and Countervailing Duties Investigating Procedure



trade. The Commerce Department would give simultaneous consideration of the sufficiency of evidence of both subsidy and injury, and decide whether to initiate an investigation within 20 days.* 56 Upon a positive determination, it continues to examine whether there is a resonable basis to believe or suspect that a subsidy exists within 160 days after the petition. On the other hand, upon a negative determination the proceeding will be closed.* 57 The ITC would within 45 days after the petition determine whether there is a reasonable indication of injury. If the determination is positive, it will suspend its proceeding until a preliminary positive determination is rendered by the Commerce Department; if negative, the whole investigating proceeding will be terminated.* 58 After a positive preliminary determination of subsidy, both the ITC and the Commerce Department would begin their investigations on the existence of a subsidy and injury simultaneously, but the time limits allowed are different: 75 days for the Commerce Department and 120 days for the ITC in reaching the final decisions.* 59 If the preliminary determinaton of the Commerce Department is negative, it will continue to examine whether there exists a subsidy, and the ITC will not begin its investigation until there is a final positive determination by the Commerce Department.* 60 Under such circumstances, the ITC is to give its final determination within 45 days.* 61 This is the only departure from simultaneity. Time is so distributed that the whole investigating proceeding would normally not exceed 12 months.* 62

(c) <u>Public Notice, Public Participation, and Access to Information</u>

The Code requires the administrating authorities to publish their decisions at each stage of the proceeding. There shall be notice of initiation of investigation to all interested parties known to the authority and a public notice in this regard,*63 public notice of any preliminary or final finding whether affirmative or negative and of the revocation of a finding, and notices of such findings to the signatory whose products are under investigation and interested exporters.*64 A notice of affirmative determination shall contain the findings and conclusions reached on all issues of fact and law considered material by the authority, and the reasons and bases for such findings.*65 A notice of negative finding shall set forth a summary of the conclusion and the reasons.*66 Reports of preliminary and final action taken with respect to countervailing duties shall be made without delay to the Committee on Subsidies and Countermeasures and shall be made available for inspection by other governments.*67 A semi-annual report of countervailing duty actions taken shall be made to the Committee.*68

An investigating authority shall upon request afford all interested signatories and all interested parties, which are defined as signatories and parties economically affected by the subsidy under investigation, a reasonable opportunity to see all the relevant non-confidential information used by the investigating authority.*69 They shall also be allowed to present their views in writing or, upon justification, orally.*70

Information which is confidential by nature or is provided on a confidential basis shall be treated as such by an investigating authority, and shall not be disclosed without specific permission of the party submitting it.*71 However, such a party may be requested to furnish non-confidential summaries and if the summarization is not possible, a statement of reasons must be provided.*72 When the investigating authority finds a request for confidentiality is not warranted, and the party making such a request is unwilling to disclose the information, the authority may disregard such information, unless it can otherwise be demonstrated that the information is correct.* 73

(d) Consultations and Voluntary Undertakings

A countervailing duty investigation does not necessarily lead to the imposition of provisional measures or countervailing duties, it can be suspended or terminated when the signatories involved have through consultation reached a mutually agreed solution or the importing country accepts voluntary undertakings by the government of the exporting country or the exporters. The Code requires the signatories whose exports are under investigation be afforded reasonable opportunities for consultations before initiation, and throughout the period of an investigation.* 74 The purposes of such consultations are to clarify the situation and to reach a mutually acceptable solution.* 75 Meanwhile, the importing signatory shall upon request permit the exporting signatory access to non-confidential evidence including non-confidential summary of confidential data being used for initiating or conducting the investigation.* 76 Consultation in such circumstances may establish the basis for proceeding under the Code's dispute settlement scheme.* 77

The government of the exporting country or the exporters may, with the intention to terminate the state of uncertainty caused by a countervailing proceeding, offer voluntary undertakings. A subsidizing government may agree to eliminate or limit the subsidy or take other measures concerning its effects, and the exporter may offer to revise their prices in order to satisfy the investigating authority that the injurious effect of the subsidy is eliminated.* 78 An investigating authority can also seek price undertakings from the exporters concerned. Price undertakings cannot be sought or accepted from exporters unless the importing country has first initiated investigation and has obtained consent of the exporting country.* 79 If the authority considers the acceptance of an offer of price undertaking impractical for such a reason as the number of actual or potential exporters is too great, it needs not to accept the offer.* 80 In the case that price undertakings are suggested by the authority, no exporter shall be forced to enter into such a undertaking.* 81 It can be inferred that the authority is obliged to accept the undertaking, if it has no reason to consider its acceptance impractical.

When a undertaking is accepted, the investigation of injury shall be terminated and there shall be no simultaneous continuation of proceedings with the implementation of price undertakings, except the government of the exporting country or the exporters desires the continuation of proceedings.* 82 If the proceedings continue and a determination of no injury or threat of injury is reached, the undertaking shall automatically lapse.* 83 However, if the determination is due in large to the existence of a undertaking, the authority concerned can require the undertaking be maintained for a reasonable period.* 84 The Code does not mention whether under such circumstances a positive determination of injury may be released from the acceptance of a undertaking and impose countervailing duties on the subsidized imports. The European Court under the pre-Tokyo Round Community's regulation has ruled that the authority could not accept the undertaking and then apply a definitive duty.* 85 The Code's rules on voluntary undertakings are designed to enable exporters or their governments to terminate the state of uncertainty accompanying a countervailing duty proceeding.* 86 The provision, granting them the right to decide whether the proceeding should be continued, is intended to protect them further if the price undertaking appears to be unnecessary.* 87 Meanwhile, the aim of the countervailing duty is to relieve domestic industry from injury rather than to penalize subsidization, and this aim can well be achieved by the acceptance of a undertaking. If the investigating authority is allowed to revoke the acceptance of a undertaking and then impose countervailing duties, the exporters as well as their governments would still be in a state of uncertainty after the acceptance of a undertaking. It may be that the latitude of the undertaking exceeds the need to, or is inadequate tc , eliminate the injury caused, because the authority may overestimate or underestimate the injury at the time it accepts the undertaking. This can be remedied by adjusting the length of time period that the undertaking is required to be maintained.

The government of the exporters from whom undertakings have been accepted may be requested by the investigating authority to furnish relevant information regarding the fulfillment of the undertakings.*88 In the case of violation of undertakings, the authority can take "expeditious actions" under the Code "in conformity with its provisions which may constitute <u>immediate</u> application of provisional measure ..."*89 That the authority is allowed to take immediate provisional measures upon violation of a undertaking may contravene the rule that provisional measures can be imposed only after a preliminry affirmative finding has been made, that a subsidy exists and there is sufficient evidence of injury.*90 This is because a price undertaking can be sought or accepted from exporters after the initiation of an investigation, regardless whether the proceeding has reached the stage of a positive preliminary finding. In the case of governmental undertakings, their acceptance is not preconditioned by the initiation of a proceeding. It may be inferred from a governmental undertaking to eliminate a subsidy or its injurious effect that there exists a subsidy and in the latter case, there is sufficient evidence of injury. However, the condition for taking provisional measures is that in all circumstances, there must be a preliminary affirmative determination that there exists a subsidy as well as that there is sufficient evidence of injury. With regard to this conflict, Paragraph 4 of Article 5 provides that the rules on violation of undertakings shall preempt those on provisional measures. It may be that the Code by allowing imposition of provisional measures without an affirmative preliminary determination intends to deter violation of undertaking. Violation of undertaking is further punished by more restrictive retroactive application of countervailing duty.*[91]

(e) Provisional Measures and Definitive Countervailing Duties

Provisional measures can be taken only after (1) a preliminary affirmative finding has been made that a subsidy exists and there is sufficient evidence of injury, and (2) the authority concerned decides that they are necessary to prevent injury during the investigation.*[92] The U.S. implementing legislation in this regard is at variance with the Code. A preliminary determination under the U.S. law is concerned about whether there is a reasonable basis to believe or suspect that a subsidy exists rather than whether there exists a subsidy, and whether there is an indication of injury.*[93] The imposition of provisional measures shall not exceed 4 months and shall be limited as short a period as possible.*[94]

The Code gives the investigating authority of an importing country the right to decide whether to impose countervailing duties and the amount of duties, when all the conditions for the imposition have been nullified.*[95] An importing country may decide not to impose countervailing duties because the subsidized imports may benefit its domestic producers using the imports as inputs, or because of the political pressure from the exporting country, or because its refraining from taking a countervailing duty action is a concession made to the exporting country in return for a benefit it has gained from the latter country. The Code also provides that it is desirable that the imposition be permissible and the duty be less than the amount of subsidy if such lesser duty would be adequate to eliminate the injury.* 96 In any case, the duty shall not exceed the amount of subsidy found to exist, "calculated in terms of subsidization per unit of the subsidized and exported product".* 97 The quoted language can be interpreted in three ways. First, the maximum amount of duty is to be calculated through dividing the gross subsidy granted by a government minus costs in obtaining the subsidy by the volume of the product, and when the grant is unevenly distributed to domestically consumed and exported products, to be calculated through dividing the net subsidy allocated to the exported products by the volume of these exported products. Secondly, the amount to be divided by the volume of the product concerned is the amount of subsidy effectively benefits the exporter. For example, a subsidy under a regional aid programme may be granted to a company to cover its costs in relocating its plant in a specific region. If the amount of subsidy does not exceed the necessary extent to cover any disadvantage that the company may suffer in relocating its plant in that region, the company would effectively benefit nothing from the subsidization. The U.S. implementing legislation, influenced by the famous Machelíne case,* 98 specifically provides that increased costs as a result of locating in an underdeveloped area cannot be substracted from the gross subsidy and they are to be included in the definition of net subsidy which forms the basis for the calculation of countervailing duties under the U.S. law. Thirdly, the duty is to be derived from dividing the amount of subsidy which affects pricing and sales efforts. For instance, exemption of a domestic direct tax upon exportation may be reflected in (1) the prices of the exported products, (2) the sales efforts, or (3) the profit-levels of the exporters.* 99 Under the assumption that direct taxes tend to be shifted backwards, it is quite possible that a part, if not all, of the benefits is absorbed by the exporters in the form of incresed profits. Since the purpose of countervailing duties is to relieve domestic producers of the importing country from injury, it is more appropriate to calculate duties on the basis of that part of subidization which may affect internatioal trade flow, i.e. those affect pricing and sales efforts. The Code does not provide any detailed rule regarding the calculation of countervailing duties, and leaves the issue to be solved by further consultation among signatories.* 100

Countervailing duties shall be applied non-discriminatorily among subsidized imports from all sources, though the duties may vary with the degree of subsidization. Retroactive application of countervailing duties is prohibited except in the following cases. First, there is a final finding of injury,* 101 as opposed to a threat of injury and a retardation of the establishment of an industry; or there is a final finding of threat of injury and the finding in the absence of provisional measures would have been a finding of injury.* 102 In both cases, countervailing duties can be retroactively applied for the period for which provisional measures, if any, have been applied. Secondly, in the case of violation of voluntary undertakings where an immediate provisional measure has been applied, countervailing duties can be imposed on goods entered for consumption not more than 90 days before the application of the provisional measures, but retroactive assessment cannot be applied to imports entered before the violation. *103 Thirdly, in the case where massive subsidized imports in a relatively short period causes injury which the authority finds difficult to repair, and it is deemed necessary to preclude the recurrence of such injury, countervailing duties can be applied to imports entered for consumption not more than 90 days before the application of provisional measures.

CONCLUSION

The lack of definition of material injury in the Countervailing Duty Code provides importing countries an opportunity to use countervailing duties as a protectionist tool. A protectionist interpretation of material injury would in turn seriously interfere with the right of other countries to use subsidies in pursuit of their national goals, and may consequently be damaging to international trade relations.

Protectionist use of countervailing duties can be furthered by interpreting the causation required as a cause rather than the cause of material injury, because of the ambiguity with regard to the Code's causation requirement.

The Code does not provide sufficient rules with reagrd to the base on which calculation of countervailing duties is to be made. If the base is to be that part of a subsidy which affects the pricing and sales efforts, protectionist use of countervailing duties can be greatly eliminated.

As subsidization by an exporting country provides cheap supply to an importing country, the latter has few economic reasons to impose counter-actions against subsidized imports. Rather, it is the social-political consequence of allowing the imports of subsidized goods that is the main reason behind governments' actions. The notion of fairness provides an important basis on which domestic producers of an importing country can establish a case of social imbalance of interest. The issue of whether subsidies are unfair will be discussed in the concluding part of this thesis. Meanwhile, subsidies may also have the effect of displacing exports from other countries in third-country markets. Such subsidies can best be handled under the Code's consultation, concilation, and dispute settlement scheme. The concluding part of this thesis will also discuss the rational way to deal with subsidies in view of their complex nature.

Footnotes (Part Two, Chapter III)

1. GATT BISD Vol.IV,pp. 10-2
2. Note 2 accompanying Article 1
3. Note 1 accompanying Article 2:1
4. Note 4 accompanying Article 2:1
5. Note 1 accompanying Article 6:1

6. Article 6:1
7. Article 6:2
8. Ibid
9. Article 6:3

10. Antidumping and Countervailing Duties, Report Adopted on 13 May 1959 (L/978) BISD 8S/145, para. 15

11. 32 Fed. Reg. 12923; TC Pub. 214 (1967)
12. Senate Finance Committee, Report onthe Trade Reform Act 1974, S. Rep. No. 1298, 93d Cong 9. 2d Sess. 185 (1974)

13. Trade Agreements Act of 1979, Pub. L. No. 96-39 101, 93 Stat. 178 (1979)
14. Congress Debate on Trade Agreements Act, Congress Record, July 10, 1979, H 5566-5567

15. International Antidumping Code, Agreement on Implementation of Article Vi of the General Agreement on Tariffs and Trade, BISD 26S/171

16. Note accompanying Article 6:1
17. see Article XIX of the General Agreement, BISD Vol.IV

18. Note 1 of Article 6:1
19. Article 6:6

20. e.g. Styrene Monomer Originating in the United States of America, Commission Regulation (EEC) No. 384/81 of 13 Feb. 1981, O.J. No. L42/14, 15; Vinyl Aeetate Monomer Originating in the United States of America, Council Regulation (EEC) No. 1282/81 of 12 May 1981, O.J. No. L 129/1,2

21. Article 6:5
22. Article 6:7
23. Ibid

24. 35 Fed. Reg. 4162; The principle was first stated in the dissenting opinion in the case of White Portland Cement from Japan, 29 Fed. Reg. 963

25. Article 6:8
26. Ibid
27. Ibid
29. Joint Group of Experts, Report to the Committee on Anti-dumping Practices and to the Committee on Subsidies and Countermeasures, SCM/M/6
30. Ibid
31. Article 6:3
32. 34 Fed.Reg. 19003 (1968); for a detailed discussion on this problem,

see Comment, "Unfair Competition---Antidumping Act Protects Domestic Portion of A Multilateral Corporation from Unfair Competition by Foreign Branch of Same Corporation", 6 Taxas Int'l Forum (1971) p.361

33. Article 6:3
34. Article 6:9
35. Article 6:4
36. Ibid
37. Note 3 to Article 6:4
38. U.S. Tariff Commission, Report... Regarding the International Antidumping Code (1968) p.12
39. Statement of Ambassador Roth, U.S. Special Representative for Trade Negotiations, U.S. Senate, Hearings before the Committee on Finance, June 27, 1968, p. 17
40. R.de C.Grey, ' The Development of the Canadian Anti-dumping System ', pp.46
41.
42. 36 Fed. Reg. 1934 (1971)
43. U.S. TC Pub. 484, May 1972
44. U.S. International Trade Commission, MTN Studies, 6 Part 1, Agreements Being Negotiated at the Multilateral Trade Negotiations in Geneva--- U.S. International Trade Commission Investigation No.332-101, pp.157
45. e.g. Vinyl Acetate Monomer Originating in the United States of America, Council Regulation (EEC) No.1282/81 of 12 May 1981, O.J. No. L129/1,3; see also Stryrene Monomer Originating in the United States of America, Commission Regulation (EEC) No. 384/81 of 13Feb. 1981, O.J. No. L42/14,15; Certain Chemical Fertilizer Originating in the United States of America, Council Regulation (EEC) No. 2297/80 of 29 August 1980, O.J. No. L231/5.7
46. Article 2:1
47. Ibid
48. Ibid
49. see the text accompanying note 31 - 34
50. Article 2:3
51. Article 5. Provisional measures can be applied only when the authorities concerned decide that they are necessary to prevent injury being caused during the period of investigation.
52. Article 4
53. Article 2:4
54. Ibid
55. Article 2:14
56. Sec 732(c) of the Tariff Act of 1930, as amended, in Section 101 of the Trade Agreement Act of 1979, Pub.L.No. 96-39, 93 Stat.178 (1979)
57. Ibid, Sec. 733 (c) (3)
58. Ibid, Sec. 733 (a)
59. Ibid, Sec. 735 (a) (1)
60. Ibid, Sec. 735 (b) (2) (B)
61. Ibid
62. see the chart following pp.110
63. Article 2:3
64. Article 2:15
65. Ibid
66. Ibid
67. Article 2:16
68. Ibid
69. Article 2:5
70. Ibid
71. Article 2:6
72. Ibid
73. Article 2:7
74. Article 3:1 and Article 3:2

75. Ibid
76. Article 3:3
77. Note 1 accompanying Article 3:2
78. Article 4:5
79. Article 4:5 (a) (ii)
80. Ibid
81. Article 4:5 (c)
82. Article 4:5 (b)
83. Ibid
84. Ibid
85. Ballbearing from Japan , cases 113/77, 118/77, 119/77 & 121/77, Luxembourg 9 March, for a detailed discussion of the present case, see Ivo van Bael,"Ten Years of EEC Anti-dumping Enforcement", J. of W.T.L. Sept. 1979
86. Article 4:6
87. Ibid
88. Article 5:1
89. Ibid, i.e. definitive duties may be levied on goods before the application of provisional measures
90. Article 5:1
91. Article 4:6
92. Article 5:1
93. Sec. 733 of the Tariff Act of 1930 as amended in Trade Agreements Act of 1979
94. Article 5:3
95. Article 4:1
96. Ibid
97. Article 4:2
98. X-Radial Steel Belted Tires from Canada , T.D.1018, 7 Cust., Bull. 11 (Jan.10, 1973), 38 Fed. Reg. 1018; The subsidy isuue involved in this case was the development assistance grants offered by the Canadian Government to attract industries to economically depressed regions. The problem was held by the U.S. Treasury as a violative subsidy. In the legislative history of the Trade Agreements Act, it was repeatly emphasized that regional incentive programmes like the one in the Michelne case should not be allowed. Congress Record, July 10, 1979; for a detiled discussion of the Micheline case, see " The Micheline Decision: A Possible New Direction for U.S. Countervailing Duty Law ", Law and Policy in Int'l Bus. Vol. 6:237 (1974)
99. see note 109
100. Note 2 accompanying Article 4:2
101. Article 4:3
102. Article 5:5
103. Article 4:6

PART TWO

LAW OF SUBSIDIES, DUMPING AND MARKET SAFEGUARD

Chapter IV

Antidumping Law

Chapter IV: Antidumping Law

Section I: Economics of Dumping

(A) Definition of Dumping

Dumping, according to the most commonly used definition, is a practice of price discrimination by a trader or a producer among different markets. In the international context, dumping is defined as selling a product in a foreign market at a price lower than the price in the domestic market. A comparison that can be made between dumping and public subsidization is that in the former case the low price of a product in a specific market is made possible by the subsidization of high prices in other markets; whereas in the latter case it is made possible by subsidization from public sources. Thus, dumping can be viewed as a kind of private subsidy as opposed to public subsidy discussed in the previous chapters. A third case can be seen when the dumping in issue is not made possible by higher prices in other markets, but rather by government subsidies. Be it enabled by public or private subsidies, dumping is generally (though arguablly) considered as an unfair trade practice, mainly because of its subsidy element. The definition that dumping is a practice of price discrimination among different markets has however partially lost its legal validity because of the emergence of the notion of fair value or normal value. Almost all modern antidumping laws adopt the notion of fair value in indentifying the existence of dumping. Domestic market prices are normally considered as the fair value, but in exceptional cases, fair value can be constructed value (i.e. cost of production and other costs plus reasonable profits) or third country prices (i.e. prices at which the same product is exported to third countries). With world recession deepening, prices below cost of production are generally considered by protectionists as not reflecting the fair value. Hence, when domestic prices are below the cost of production, they are disqualified as fair values. This is so, even though below-cost pricing is a common practice in some sectors faced with excess capacity and inadequate demand and with high fixed production costs. Such a rule, in effect, regards all sales below average costs as dumping because under such circumstances the actual sales prices are facing constructed value as fair value. This is so regardless of whether there involves price discrimination. The change in the definition of dumping also affects the validity of the underlying rationale for treating dumping as an unfair trade prctice.

(B) Prerequisits for Practicing Dumping

A trader's ability to practice dumping in foreign markets is subject to the following conditions. First, consumers in the dumped market are more sensitive to price fluctuations than consumers in the domestic market. Secondly, the dumper has some degree of market power in controlling the supply of the dumped goods in the domestic market. Usually this condition can be satisfied when the dumper is an oligopolist or a monopolist in his domestic market. The condition can also be satisfied by the forming of a cartel among producers in the dumper's home market. This condition can be substituted by export subsidies from the dumper's government. Thirdly, the dumper can avail himself of natural or artificial barriers in preventing the importation of, and in isolating his home market from world markets for, the dumped goods. Those barriers include transportation fees, high import tariffs, quotas, unique designs for exported products and other non-tariff trade barriers.

(C) Classification of Dumping

In his classic study of dumpimg, Viner, taking into account of the motivation behind dumping, classified dumping into three categories: sporadic, short-run and long-run dumping. Sporadic dumping occurs (1) when the dumper is seeking to dispose of a casual overstock in order to avoid the reduction of prices in his primary markets, (2) when he exports the goods upon a speculative calculation of profitable price, or (3) when the delivery of the goods for some mistakes is unable to make the original purchases. Short-run or intermitten dumping takes place when the dumper endeavors (1) to establish trade connections and to gain goodwill in a new market, (2) to maintain connections in a market where prices are on remaining conditions unacceptable, (3) to cripple other competitors and therefore to eliminate competition, (4) to forestall the development of competition in the dumped market, or (5) to retaliate against dumping in a reverse direction.*1 Long-run dumping can be seen when the dumper is making efforts to maximize his profits through the maintenance of full production from existing plant facilities or through the attainment of economies of scale without cutting prices in his primary market. In support of Viner's classification, Fisher explained that the marginal cost was zero in sporadic dumping, possibly above marginal revenue (price charged in the dumped market) in short-run dumping, and always equal or below marginal revenue in long-run dumping.*2 Whether the price charged in the dumped market is below marginal cost is used by many as the test in identifying the dumper's predation to eliminate competition in the dumped market. By using the trade effects of dumping as the criterion, Barcelo classified dumping into <u>per se</u> and injurious dumping. Injurious dumping is subcategorized into predatory injurious and non-predatory injurious dumping. <u>Per se</u> dumping is defined as dumping which causes only minimal injury to competitors in foreign markets. Injurious dumping refers to dumping which causes "such pervasive injury to domestic competition as to threaten monopolization".*3

Viner considered that only short-run or intermitten dumping was objectionable to an importing country, because such dumping was supposed to result in injury to domestic industry greater than consumers' gain.*4 Consumers' gain in the case of sporadic and long-run dumping is presumed to outweigh injury to domestic industry. Fisher held the view that not only short-run dumping, but also long-run dumping which was made possible by various trade barries to prevent re-importation of dumped goods and resulted in unemployment in the importing country and misallocation of world resources should be condenmed.*5 Barcelo, who took the most liberal position, argued that only predatory injurious dumping was objectionable. Other types of dumping are normal trade practices and beneficial to both world economy and the importing country, largely because of the consumers' surplus in the markets outside the dumper's home market.*6 The impact of dumping on world economy and the importing country concerned will be examined in more detail in later sections.

Dumping by state-controlled-economy countries presents another pattern. As the production in these countries is centrally planned, it may result in occasional surpluses which must be disposed of outside the domestic markets.*7 Moreover, since prices in these economies are not determined by market forces, they are in a more favourable position to practice price discrimination , theoretically subsidized by all resources available in the economies.*8 Being thus equipped, they are inclined to undercut prices in foreign markets in order to obtain foreign currencies to finance their imports of high technology goods from western countries.

Dumping by developing contries also has its characteristics. Like state-controlled-economy countries, developing countries need foreign currencies to finance their development projects. Governments often intervene in the economies to remedy the deficiency of market forces. The cost structure of the export sector in these countries is usually different from that of the domestic sector. For instance, the tax burden of the exported goods may be lighter than that of the domestically consumed goods, and exported goods produced in the free trade zones may be cheaper because of less administrative complications and less stringent government regulations. Under such circumstances, prices at which a product is sold in the international markets are usually lower than the prices of the same product in the domestic market. Moreover, producers in those developing countries, using high tariffs and other barriers to foster import substitution and industrialization, must practice dumping in order to be competitive in world markets, in so far as those goods using imported components are concerned. *9 Meanwhile, with the protected home market and dumping abroad, the increased domestic price and the lower dumped foreign price may more closely reflect the true scarcity of foreign exchange which cannot be reflected if a devaluation is employed.*10 Of all the three arguments mentioned above, only the first one based on the difference in cost structures is accepted by the GATT as a basis for granting preferential treatment to dumping by developing countries.

(D) Dumping in the Light of Efficiency

In this discussion of efficiency effect of dumping, the term "dumping" is used in the conventional sense, i.e., price discrimination between domestic and foreign markets.

Global efficiency in the allocation of resources can be best achieved, when there is vigorous competition across national boundaries, and in the domestic markets of individual trading nations.

In the dumper's home market, the state of competition would not be significantly worsened or improved by his practicing dumping in foreign markets. The dumper is unlikely to raise domestic market prices to a level that potential competitors would enter into the market. In order to finance the dumping, he may use accumulative reserves or external financing.*11 In the case that the prices he charges in the dumped market are above the long-run marginal cost, there is no out-of-pocket sale and therefore no need to seek financial subsidies.*12 Moreover, competition in the home market will not be worsened by the existence of dumping, because the market is already a monopolistic one.

In the dumped market, the concern is whether more or equally efficient competitors in that market will be driven out of the market or crippled. A classic argument against dumping is that the dumper, benefited from monopoly position in his home market, is able to undercut prices in the dumped market, and thus drive more efficient competitors out of the market. The issue thus to be examined is when a more efficient competitor would be in danger of being excluded from the dumped market. In this regard, there is the controversy as to whether marginal cost of production should be the test in identifying the dumper's predation to eliminate competition in the dumped market. Phillip Areeda and Donald Turner suggested that, only sales below short-run marginal cost be presumed to be anti-competitive.*13 This is because marginal cost pricing is the right strategy to maximize profits or minimize losses during a period of excess capacity and inadequate demand, and the same policy in a period of full capacity utilization is unlikely to have predatory effects. Since marginal cost is difficult to identify, they suggested average variable cost to be the test. This test, however, fails to exclude firms whose production pattern is labour-intensive and therefore have a higher average variable cost than those less efficient firms with a capital-intensive production pattern, i.e. with higher long-run marginal cost, in the same industry..*14 Another approach to identify predation is to consider sales below average total cost, used as a proxy for long-run marginal cost, as anti-competitive. This approach would consider a large amount of profit-maximizing sales in a recessionary period as dumping, and encourage cartel pricing in a recessionary period. No matter whether the test is short-run or long-run marginal cost, one can be sure that dumping is not necessarily anti-competitive. Only those sales at prices below marginal cost (long-run or short-run) are likely to be anti-competitive.

In some cases, dumping can have pro-competitive effects in the dumped market. When the dumped market is subject to collusive or inter-dependent pricing, dumping can bring prices nearer to competitive levels. Moreover, when entering into a new foreign market, an exporter may find it necessary to reduce his price in order to overcome the pre-existing trade relationships.

(E) Dumping in the Light of National Welfare

Exporting Country : It is apparent that a monopolist in the domestic market of an exporting country must foresee some kind of benefit in practicing dumping abroad. And in most cases, the benefit would materialize.

In determining whether an exporting country as a whole gains or loses from dumping, one also has to examine the dumping effect on its domestic consumers and users. In comparing dumping with simple monopoly, one conclusion was drawn by Robin that the slope of the demand curve in the exporting market would usually result in increases in output and dumping is likely to reduce the market price of the exporting country, when the marginal cost is falling with increases of output.*15 When the dumped commodities are raw materials or intermediate goods, producers in the home market using the dumped goods as inputs are at a disadvantageous position in competiting with foreign producers benefiting from the cheap dumped imports. For mutual benefits, the dumper may compensate those home-market user-producers by offering rebates for their exports. In the case that the low foreign market prices are resulted from competition among producers of the exporting country, they may cartelize their export activities in order to improve the exporting country's terms of trade. The exporting country can benefit more by forming an export cartel in the case of reverse dumping where, in additon to the improvement in terms of trade, home market consumers benefit from low prices because of the competition among domestic producers.*16

Importing Country : The producers in the dumped market, of course, would suffer loss of business, unless they bring their prices in line with the dumper's price. As a result, dumping may force those producers to idle their plants or impose on them adjustment costs in shifting to other industries and in shifting back when dumping ceases in the case of intermitten (short-run) dumping. Sporadic dumping is too short to be significantly injurious to producers in the dumped market. In the case of long-run dumping, these producers have to shift resources to alternative uses . The importing country would not suffer from the adjustment process, if it has a frictionless, full employment economy. However, adjustment process could be slow and socially painful during a recessionary period. It is often argued that in recession, employment and other effects of dumping outweigh consumers' benefits from cheap imports, and the welfare gain of the importing country from dumping is therefore negative.

In long-run and sporadic dumping, consumers and user-producers in the dumped market would benefit from cheap dumped imports. When dumping is predatory in nature, it is argued that the present low prices will be offset by future high prices, because the dumper after having gained a dominant position needs to raise prices to recoup the loss incurred in eliminating other competitores. However, predatory dumping is particularly unlikely to suceed at the international level. It is difficult for the dumper to estimate the price to charge in the dumped market in order to eliminate competitors from all over the world, and even if he suceeded, to maintain his dominant position. Intermittent or short-run dumping is also usually considered objectionable in the light of consumer welfare because it may eliminate some competitors and therefore result in higher long-term prices. However, it is unlikely that other competitors will be deterred by dumping, if they can foresee the opportunities for lon-run supply. The true concern about intermittent dumping is its effects on the variability of prices and the uncertainty concerning future prices. Such dumping is likely to result in lower mean price over a period than without duming, even when it increases the variability of the price of the dumped goods.*17 Under such circumstances, an economy is more likely to gain from trade possibilities under uncertainty.

(F) Arguments for Strict Control on Dumping

The most frequently used argument against dumping is that the advantage that a dumper has in practicing price discrimination is artificial rather than genuine. Dumping is an unfair trade practice because the lower dumped prices are subsidized by higher dumper's home market prices. Such subsidization is unjustified, because dumping exploits the evils of monopoly power which are socially undesirable for it allows the monopolist to restrict his output to reap high returns.*18 Moreover, in the case of short-run dumping, consumers in the dumped market, though benefited from present low prices, may have to pay high prices in the long run. The resulting adjustment problem of dumping is difficult to solve in recessions and the social costs would outweigh the consumers' gains. Finally, in the case of cyclical dumping, cut-throat competition between the dumper and other competitors in the importing market may be wasteful and lead to serious inefficiency.

(G) Arguments for Liberal Control on Dumping

Liberal traders often argue that dumping is in most cases not contradictory to free trade and its welfare effect on the importing country is positive. Thus, except in the case of predatory dumping, there is no need for an importing country to impose restrictions on dumped imports. In reply to arguments against dumping, they developed the following counterarguments. First, the comparative advantage that the dumper has is genuine rather than artificial, and the accusation that dumping is subsidized by high home market prices is not well founded. So long as the dumped price is above marginal cost, dumping is cost-justified. In such a case, the dumper is maximizing his profits or minimizing his losses, and one cannot say that the low pricing in the dumped market is artificial or uneconomic. In other words, marginal cost rather than average total cost should be the test in deciding whether the low price is cost-justified. The monopolistic home market only facilitates dumping rather than subsidizes dumping.*19 Secondly, that dumping exploits the evils of monopolistic power is of no concern of antidumping law or any international law. If consumers in the dumper's home market are in fact exploited, it is the existence of monopoly power rather than dumping which is to be blamed.*20 The proper mechanism to correct such a distortion is the antitrust law of the dumper's home country. In addition, there is still the possibility that home market prices will be reduced as a result of dumping. Thirdly, although the impermanence of dumping may impose injurious adjustment costs, more weight should be given to the pro-competitive effects of dumping which may in turn be beneficial to the control of inflation in the importing country.*21 Fourthly, although consumers or user-producers in the importing market would be faced with uncertainty about future prices, it is possible for the country to gain from trade under uncertainty.*22 With regard to cyclical dumping, its damaging effects apply equally to exports under uniform pricing. Moreover, except in the great depression of the 1930s, cut-throat competition appears to be rare.*23

Liberal traders conclude that, except predatory dumping and to some extent cyclical dumping, dumping should not be condemned. Antidumping legislations are superfluous, because predatory dumping can be dealt with by the application of antitrust law of the importing country and cyclical dumping seldom leads to cut-throat competition which also occurs in the case of uniform pricing. If it is impossible to abolish antidumping law, the law must be so modified that only dumping which causes injury to competition in the importing market is to be condemned.*24

(H) <u>An Overall View</u>

In reaching a verdict on dumping, one has to consider the following questions: (1) whether dumping is pernicious to global efficiency, (2) whether the importing country as a whole benefits from dumping, and (3) whether dumping is an unfair method of competition. As discussed in this section, with the exception of predatory and cut-throad cyclical dumping, global efficiency is not likely to be adversely affected by dumping, when the dumper's monopolistic position in his home market is treated as a given factor of competition. In connection with the national welfare of the importing country, most economists agree that dumping is more likely to have positive effects on consumers' welfare. However, the adverse effects on the domestic industry are argued by many to outweigh the benefits to consumers in a recessionary period involving cyclical as well as structural changes in the economy. Since the welfare effect on the importing country as a whole is uncertain, the third question that whether there is unfairness in dumping practices becomes crucial in determining whether to impose restraints on dumped imports. Two issues are to be considered in regard to the third question. They are (1) whether the low prices in the dumped market are subsidized by high prices in the dumper's home market, and (b) whether the competitive advantage that the dumper has as a result of his home market condition is justified. With regard to the first issue, when the dumping prices are below short-run marginal cost, there must be a subsidy, but the subsidy may be from accumulated reserves or external financing other than high prices in the dumper's home market. When the dumping prices are above short-run marginal cost but below long-run marginal cost, there also ought to be a subsidy possibly from high profits from cyclical upturns and/or high prices of the home market. When the dumping prices are above long-run marginal cost but below long-run average total cost, there is no need for a subsidy because the dumped goods are not sold at a loss. In such a case, the industry concerned is benefited from economies of scale, and the monopolistic home market is faciliating rather than providing subsidies to dumping. The follow-up question is whether such facility is a justified source of comparative advantage. A dumper's monopolistic position in his home market may be the result of his government's failure or unwillingness to enforce antitrust regulations. Comparative advantages of this kind, like comparative advantages derived from lower pollution control standards, are in most cases less justifiable than those derived from high technology or abundance in energy resources. From the viewpoint of absolute global efficiency, such comparative advantage should not be allowed. However, in the absence of a proper mechanism such as an effective antitrust regime in the exporting country, one may choose to tolerate the existence of such distortion rather than to approve the use of antidumping restrictions which may well create further distortion. This is particualrly true when the welfare gains of other countries than the exporting country are positive. It is therefore possible that the concept of fairness would be in conflict with maximization of global welfare. For national governments, the voice for fairness from domestic sectors adversely affected by dumping is always louder than that of other interest groups in times of economic hardship. Antidumping legisltions were thus enacted with the concept of fairnes as the main underlying rationale.

Section II: Antidumping Law under the GATT System

(A) Introduction

Dumping is dealt with in Article VI of the General Agreement, which reads:

> "The contracting parties recognize that dumping, by which products of one country are introduced into the commerce of another country at less than the normal value of the product, is to be condemned if it causes or threatens material injury to an established industry in the territory of a contracting party or materially retards the establishment of an industry ..."*25

Normal value of a product is usually the price of the like products in the exporting country; or, in the absence of such a domestic price, the highest price for the like products for export to any third country or the cost of production plus a reasonable addition for selling cost and profit. Both the domestic price and the third country price shall be prices in the ordinary course of trade. Due allowances shall be made for differences that affect price comparability. Antidumping duties can be levied to prevent or to offset dumping, but the amount of duty shall not exceed the margin of dumping. Contracting parties are not bound to comply with Article VI when their pre-existing national antidumping legislations are in conflict with Article VI.

In the 1960s, the use of antidumping measures was increasing and it was felt that antidumping action rather than dumping itself was becoming a barrier to trade. The issue was discussed in the Kennedy Round negotiations, and the outcome was the GATT International Antidumping Code of 1967, which was intended to implement the antidumping part of Article VI. A Committee on Antidumping Practices was established to review the operation of national antidumping laws. In the Tokyo Round negotiations, the 1967 Code was revised. Those articles in the 1979 Code regarding the determination of injury, and administrating procedures are essentially the same as their counterparts in the Subsidy/Countervailing Duty Code of 1979 which has been discussed in the previous chapters. The revised International Antidumping Code differs from the original code in the following areas. (1) The causal requirement between dumping and injury under the 1967 Code was principal causation, whereas the requirement was replaced by simple causation in the 1979 Code.*26 (2) With regard to the definition of regional industry, the demand in regional market under the 1979 Code needed only be "not to a substantial degree" supplied by producers located elsewhere, whereas under the 1967 Code "none or almost none" of the demand in the regional market is supplied by outsiders.*27 (3) A written request is required for the initiation of an antidumping investigation proceeding under the 1979 Code, whereas there was no such requirement under the 1967 Code.*28 (4) Under the 1979 Code, when requesting for confidential treatment to information supplied to the investigating authorities, the supplying party shall demonstrate the causes; whereas this was not necessary under the 1967 Code.*29 (5) The 1979 Code extends the time limits for application of provisional measures from 3 months to 4 months.*30 (6) The 1979 Code also provides special rules in regard to developing countries.*31 (7) The 1979 Code formalizes the dispute settlement scheme and the Committee on Antidumping Practices which functioned infomally under the 1967 Code. The new Code also emphasizes the desire for a speedy, and equitable resolution of disputes.*32 (8) The new Code prohibits retroactive assessment 120 days prior to complaints when appraisement of duties was withheld for reasons unrelated to dumping, whereas this was allowed under the 1967 Code.*33

As the rules on determination of injury and the ~~producers~~ in the antidumping administration are the same as those in the countervailing duty administration, discussions in the following will concentrate on the determination of dumping and its related issues under the new Code (hereafter the Code).

(B) Determination of Dumping

Since dumping is defined as selling a product in a foreign market at a price below its normal value, two figures are of primary importance: the export price of the product and the normal value. After the determination of these prices, they shall be subject to further adjustments in order to accomplish a fair comparison at the same level of trade, usually the ex-factory level. Since the Code does not provide detailed rules regarding the determination of dumping, especially the determination of the prices to be compared with, the following discussion is mainly based on the U.S. antidumping law and regulation, supplemented by those of the EEC and Canada.

(1) Export Price

The Code does not specify how the export price shall be determined, except in the case of sales between related parties and sales under compensation agreements. Under the U.S. law, the export price can be the purchase price or the exporter's sales price. The purchase price is "the price at which mechandise is purchased or agreed to be purchased, prior to the date of importation, from the manufacturers or producers of the mechandise for the exportation to the United States." *34 The rule that the purchase price shall be the price agreed prior to the importation rather than the exportation is intended to accomdate the situation where the price changes after the exportation and before the importation of the mechandise in question due to, say, currency fluctuations.*35 The exporter's sales price is " the price at which the mechandise under investigation is sold in the U.S. before or after the time of importation by or for the account of the exporter."*36 To make the purchase price or the exporter's sales price comparable to the home market price at the ex-factory level, some additions and deductions shall be made. The selected base price shall be increased by cost of all containers and coverings and all other packing costs for shipment to the U.S.*37 The exporter's sales price is subject to two further deductions: (1) any increased value resulting from a process of the merchandise after importation,*38 and (2) the commission for selling in the U.S.,*39 and (3) selling expenses generally incured by or for the account of the exporter.*40 The Canadian antidumping law has similar rules in this regard to those of the U.S. except that the exporter price shall be the lesser of the exporter's sales price and the importer's purchase price after being duly adjusted.*41 The EEC antidumping regulation stipulates that the export price shall be the price actually paid or payable for the product exported to the Community.*42

When the base price selected for the determination of the export price appears unreliable because of association or a compensation arrangement between the exporter and the importer or a third party, the Code allows the export price to be constructed on the basis of the price at which the import in question is first resold to an independent buyer.*43 When the import is not resold to an independent buyer or not resold in the condition as imported , the export price can be constructed on such reasonable basis as the administrating authorities may determine.*44 Under the U.S. law, the exporter's sales price is used in such a case.*45 The Canadian law requires the use of the price at which the goods in question are sold to an unrelated person as the base price to be adjusted by appropriate allowances similar to those applicable to the U.S. exporter's price.*46 The Community's regulation is more or less the same as the Code and provides allowances for items similar to those in the case of the U.S. exporter's price.*47

(2) Normal Value

According to the Code, normal value can be (1) the home market price (in the country of origin), (2) the price in the exporting country's market (when the product is not exported directly from the country of origin), or (3) the export price for a third country or (4) constructed value, when there is no appropriate home market price.

(a) Home Market Price

Home market price is the price, "in the ordinary course of trade, for the like products when destined for consumption in the exporting country"*48, when the product in question is directly exported from the country of origin.

(i) Like Products : The term "like product" in the antidumping context is defined in the same way as in the determination of injury in the countervailing duty context, i.e. "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, although not alike in all respects, has characteristics closely resembling those of the product under consideration."*49 The U.S. Court of International Trade in Portable Electric Nibblers from Switzerland *50 took the view that the "concept of likeness of a product does not require exact identity, but does require that goods be substantially the same in uses or characteristics."

(ii) Ordinary Course of Trade : The Code gives no definition as to what constitutes "the ordinary course of trade". The U.S. law defines the term as "the conditions and practices which, for a reasonable time prior to the exportation of the merchandise which is the subject of an investigation, have been normal in the trade under investigation..."*51 A firm's practice may constitute dealing in the "ordinary course of trade", even if all of the other firms have different practices, when the firm accounts a sizeable market share and had been doing business in that manner for sometime.*52

(iii) Destined for Home Consumption : In an early case, the U.S. Court of Customs and Patent Appeal held that home consumption means the destruction of an article in the country of its production by use or conversion into another manufactured product.*53 In a more recent case, the U.S. Treasury placed more emphasis on whether the producer knew or should have known that the sales were destined for export. If positive, the sales in question would be excluded from normal value calculation.*54

(iv) Selection of Base Price : (1) Time. The U.S. law stipulates that the base price for the determination of foreign market value (home market value) shall be the price of the similar merchandise at the time of exportation of the product under investigation to the U.S., when the export price to be compared with is the exporter's sales price.*55 The base price shall be ascertained as of the date of the purchase or agreement of purchase when the export price to be compared with is the purchase price.*56 Under the Canadian law, the base price shall be the price during the period in relation to the sale of goods to the importers in Canada.*57 (2) Place. Under the U.S. law, the base price shall be the price in the principal markets of the country of origin;*58 whereas under the Canadian law, at the place the goods were or would be shipped directly to Canada.*59 (3) Quantities. The U.S. law requires that the selection of base price shall be based on the usual wholesale quantities. *60 (4) Market Condition. The Canadian law provides that the base price shall be determined under competitive conditions.*61

(v) Adjustment to the Ex-factory Level : After the selection of the base price, the price shall be adjusted to a price at the same level of trade as the export, normally the ex-factory level. When not included in the base price, adjustments are to be made for the cost of containers and coverings and all other charges and expenses necessary for placing the product in condition ready for shipment to the importing market concerned.*62

(b) Price in the Exporting Country other than the Country of Origin

When the products concerned are exported from an intermediate country rather than the country of origin, normal value shall be based on the price in the market of the exporting country.*63 This rule, however, is not applicable to the situation where the products are merely trans-shipped through the country of export; or such products are not produced, or there is no comparable price, in the country of export. Under these circumstances, the price in the country of origin shall be used as the base price.*64 The Code again gives no rules regarding the selection of the base price in the country of export. Under the U.S law, the rules are the same as those for the selection of home market price.

(c) Third Country Price

It is possible that there are no appropriate prices in the exporting country's market (including the home market) to be used as the base price, either because there are no sales of like products in the ordinary course of trade in that market, or because sales in that market do not permit proper comparison due to its particular market situation. In such cases, the Code allows the use of the export price to any third country or constructed value as the basis for comparison.*65 Such export price for the purpose of comparison may be the highest among all export prices to third countries, so long as it is a representative price.*66 In selecting the proper third country, the U.S. law requires that preference be given to the country the product exported to which has a greater degree of similarity than those exported to other countries, provided the volume of sales to such a country is deemed adequate; then, to the country the volume of sales to which is the largest among those sales outside the home market or the United States; and thirdly, to the country the market of which is most like the United States market, in terms of organization and development.*67 When a single country does not provide adequate sample, sales to additional countries selected according to the above criteria may be aggregated.*68 The price so selected shall be the price at the exportation of the product concerned.*69

(d) Constructed Value

The calculation of constructed value is based on the cost of production in the country of origin plus reasonable amounts for administrative, selling and any other costs and for profits. Generally, the profit rate used in the calculation of constructed value shall not exceed that normally realized "on sales of products of the same general category in the domestic market of the country of origin".*70 This rule is intended to prevent the use of profit rate of sales in the market of the importing country so that antidumping duties would not be used as a protective means by raising the profit level to the extent not lower than that of the producers in the exporting market. However, the Code does not make this rule mandatory and allows signatories to evade the rule by claiming that sales at lower profit levels or at zero profit are not in the "ordinary course of trade". The U.S. law makes it mandatory that general expenses which form a part of the cost of production be not less than 10% of the cost of materials, fabrication and processing, and, more importantly, the reasonable profit be not less than 8% of the total cost.*71 Packing cost for shipment to the exporting market concerned shall be included in the constructed value.*72

(3) Necessary Adjustments in Making Comparison

In comparing the export price with the normal value, the Code requires that due allowance be made "in each case, on its merits, for the differences in conditions and terms of sales, for differences in taxation, and for the other differences affecting price comparability."*73

(a) Difference in Taxation

The main differences in taxation between exported goods and domestically consumed goods are resulted from border tax adjustment and border tax. In order to make the export price comparable to the homemarket price, the U.S. law stipulates that the amounts of the following items are to be added to the export price: (1) import duties on materials by the exporting country which have been rebated or uncollected,*74 (2) any tax imposed by the exporting country on exported merchandise which have been rebated or uncollected, but only to the extent that such taxes are added to or included in the price of such or similar merchandise when sold in the exporting country,*75 and (3) the amount of countervailing duties imposed on the merchandise to offset an export subsidy.*76 Moreover, any export tax, duty or other charge imposed by the country of exportation shall be deducted from the export price, but this does not apply to export taxes, duties or other charges levied specially intended to offset the subsidy received by the merchandise exported to the U.S.*77 In the computation of constructed value, internal tax imposed by the exporting country on materials upon their importation but refunded or remitted upon exportation of the products using such materials as inputs shall be excluded.*78

(b) Difference in Conditions and Terms of Sales

Such differences can be differences in credit terms, guarantees, warranties, technical assistance, servicing and the assumption by a seller of a purchaser's advertising or other selling costs. The Code provides no rule on the extent to which adjustments are allowed with regard to these items. The U.S. law requires all adjustable items shall be directly related to sales under consideration.*79

(c) Other Differences

Differences may also arise from salaries and/or commission paid to salesmen, warehousing expenses, reserves for bad debt cost, or even elements of seller's overhead and general expenses. The Code does not provide the extent to which adjustments for differences can be allowed. The U.S. law in this regard stipulates that only differences which bear direct relationship to the sales under investigation and affect market value of the merchandise shall be considered.*80 In application, the U.S. Treasury in pre-Tokyo Round cases adopted a rather restrictive approach. Salaries paid to salesmen and overhead costs associated with the maintenance of large warehousing facilities, the maintenance of a large sales force within the producer's country, and reserves for bad debts were all disallowed as adjustable items.*81 The 1980 Commerce Department's Regulation liberates the rule to some extent by allowing these items except elements of overhead and general expenses to be adjustable.*82 The rationale for disallowing elements of overhead and general expenses may be that adjustable items shall be those directly affect the particular sale under investigation rather than those can be allocated to all sales.*83 However, it is possible that the manufacturer concerned maintains a large distribution system in his home market, but a minimal one in the foreign market, and this difference is usually allowed in normal accounting practice.*84

Difference may also arise from natural disadvantages of foreign producers in competiting with producers in the importing market, such as uncertainty in supply, irregular schedules, difficulties in making adjustments for damaged or defective merchandise, lack of contact between customers and suppliers and the natural preference for domestic goods. These differences are all likely to affect the value of the product concerned in the importing market. Difference in quantities may also affect price comparability, because prices may vary with the quantities of sales. Adjustments are allowed for such difference under the U.S. law, provided (1) the price differential is wholly or partially due to differences in quantity, and (2) such quantity discount is a normal trade practice of the industry in the exporting country.*85 Moreover, the exporter has to prove that he had granted the same quantity discount to at least 20% of his home market sale or export sale to third countries for six months before the presentation of dumping complaint, or to demonstrate that the discount is warranted by cost saving.*86 The U.S. law also allows adjustment for differences in physical characteristics.*87 The EEC law regarding adjustments is almost the same as the U.S. law.

(C) Determination of Dumping by State-Controlled Economy Countries

Article VI of the General Agreement recognizes that "in the case of imports from a country which has a complete or substantially complete monopoly of its trade and where all domestic prices are fixed by the State, special difficulties may exist in determining price comparability ..." and that under such circumstances, a strict comparison with domestic prices may not always be appropriate.*88 However, both the Code and Article VI give no guidance as to the determination of normal value in regard to exports from state controlled economy countries. It is possible, under the Code, that domestic sales in, or foreign sales by, state-controlled-economy countries are not in the ordinary course of trade as understood in the market economies, and therefore these sales are disqualified as the basis for the determination of normal value. It is also inappropriate, from the viewpoint of a market economy, to construct the normal value by using the domestic market of a state controlled economy country as the reference market, since prices of components and labour costs are not determined by market forces either. Under the U.S. law, the reference market for the selection of the proper base price for the determination, or constructing, of normal value is shifted from the domestic market of a state controlled economy country (either as a country of origin or only as a country of export) to the domestic market of a third non-state-controlled economy country.*89 In selecting the proper third non-state-controlled economy country, preference is given to such country with its stage of economic development comparable to that of the state-controlled economy country in question.*90 If no such a country can be found, another non-state-controlled economy country other than the U.S. can be used, with due adjustments for differences in the costs of material and labour.*91 The comparable economic development approach is criticized as not reflecting the difference in comparative advantage that might exist between the exporting country and its substitute country.*92 The adjustment approach, though making an effort to reflect such difference, may prove to be unworkable as the price and cost differences between a state-controlled economy and a non-state-controlled economy are difficult, if not impossible, to determine. Finally, when the above two approaches do not provide adequate basis, the U.S. market can be used for the purpose of determining the price or constructed value.*93

The Canadian law leaves the issue of exports from state-controlled-economy countries to the discretion of the administrating authority without providing any other special rule.*94 The EEC antidumping regulations adopt the same approach as the U.S.law, but without specifying to which third market economy country priority should be given. The price paid or payable in the EEC can also be used as a last resort, if the price is duly adjusted to include a reasonable profit margin.*95

One difference between the U.S. and EEC and Canadian antidumping legislations in regard to exports from non-market-economy countries is that the latter two consider that special situation exists when encountering products from any non-market-economy country. The U.S. law, however, recognizes the existence of special situation only when the economy of the exporting country in question "is state-controlled to an extent that sales or offers of sales of such or similar merchandise in that country or to countries other than the United States do not permit a determination of" normal value by using the rules applicable to market economy countries.*96 Thus, the emphasis is the degree of state-control rather than the fact of state-control. In Menthol from the People's Republic of China,*97 the Commerce Department found the existence of a special situation that required the application of state-controlled-economy rule. This is because the economy of the PRC is state-controlled both in aggregate and in agricultural sector based, in part, on general limitations on transferability of land and labour in the PRC and indirect effects that pervasive controls on other agricultural products necessarily have on menthol production. In a meeting of the Committee on Antidumping Practices on 3-4 April 1978, the U.S. representative assured that the U.S. would not apply and had not applied the state-controlled-economy rule to exports from state-owned firms in market economy countries.*98

(D) Determination of Dumping in the Case of Developing Countries

As mentioned previously, exports from developing countries may be sold at price below their home market prices, because of the emhpasis they place on exports. Export subsidies and other promotional measures are common practices to boost exports, and they often result in dual pricing. Developing countries have long been arguing for special treatment concerning determination of dumping, and the Brazilian Proposal which voiced the demands of developing countries for GATT reform urged the use of export price to third countries in stead of home market price as the normal value in determining dumping when exports from developing countries are in issue.*99 The Tokyo Round negotiations failed to settled the issue in concret. The new International Antidumping Code in its preamble expresses that the particular trade, development and financial needs of developing countries have been taken into account in drafting the Code.*100 Article 13 of the Code provides that "Possibilties of constructive remedies provided for by the Code shall be explored before the the applicaion of antidumping duties where they would affect the essential interests of developing countries."*101 "Possbilities of constructive remedies" could mean price undertakings by the exporters or importers, or negotiation of a mutually acceptable solution between two countries concerned under the Code's dispute settlement scheme. In a 1980 report on decisions adopted by the Committee on Antidumping Practices, more detailed guidelines with regard to developing countries are provided.*101 In that report, it is stated that the Code is not intended to prevent government interventions in developing countries, which may result in different economic regimes for exports and domestic trade, as long as those government measures are used in a manner consistent with the General Agreement. However, whether developing countries can actually benefit from this decision is very much in doubt. That exporters in developing countries sell their manufactures at prices lower than the domestic prices is in most cases made possible by export subsidies from their governments. Export subsidies in the case of developing countries, according to the Subsidy/ Countervailing Duty Code, though free from countermeasures at the GATT level provided there exists a commitment to eliminate subsidies when they are not necessary for development purpose, are still subject to countervailing duties. Thus, even the exports in question can escape from the imposition of antidumping duties, they would still be encountered by countervailing duties. The first part of the second decision in the same report is also superfluous. It stipulates that the fact that the export price is lower than the home market price "does not per se justify an investigtion or the determinaion of dumping unless the other factors mentioned in Article 5 are also present."*103 Article 5 of the Code sets the conditions for the initiation of antidumping investigating proceeding, which include sufficient evidence of (a) dumping, (b) material injury, and (c) a causal link between dumping and injury. The mere existence of dumping under Article 5 is not sufficient for initiating an investigaion, and the second decision in this regard only repeats the rule.

The latter part of the second decision is more important. It requires considerations be given to all cases where home market prices do not provide commercially realistic basis for dumping calculation, because of special economic conditions.*104 Under such circumstances, the export prices for third countries or the price constructed in the home market shall be used as the basis of normal value.*105 It is unclear whether government subsidies shall be excluded from the calculation of the costs, including production, administrative, selling and any other costs. If not, when export subsidies are considered as an element of developing countries' economies, and the main difference between the home market price and the export price is resulted from such subsidies, the home market price could still be the basis of normal value, provided due adjustments are made to reflect the subsidy element in the export price. Only when the difference is resulted from factors that can not be quantified such as government regulations restricting the level of supply for domestic consumption, or the difference is not allowed for adjustment under national antidumping legislations, there is a need for this special rule, i.e. using the export price for third countries or constructed value as the normal value.

(E) Determination of ~~Dumping~~ Injury

The Code's provisions on the determination of injury are essentially the same as their counterparts in the Subsidy/Countervailing Duty Code. Thus, the discussions on the determination of injury in the last chapter are also applicable to the present discussion on antidumping duties.*105

(F) Investigating Procedures and Evidence

Readers are referred to the discussion on the procedural rules of the Subsidy/Countervailing Duty Code in the last chapter.*106

(G) Price Undertakings

One of the alternative remedies to countervailing duties, as discussed in the last chapter, is voluntary undertakings by the exporters concerned or by their governments.*107 Voluntary undertakings, in the context of countervailing duties, can be price revision by the exporters or elimination of the subsidy or its effects by the exporters' governments. In the case of dumping, a manufacturer's price discrimination practice does not directly involve the activities of his government, and therefore price undertakings by exporters is the only form of voluntary undertaking. The rules governing the use of price undertaking as an alternative remedy to antidumping duties are the same as those in the Subsidy/Countervailng Duty Code.*108

(H) Provisional Measures, Imposition of Antidumping Duties and

Retroactivity

The Code's provisions in these regards are again similar to those of the Subsidy/Countervailing Duty Code, except the following cases. First, antidumping duties shall not exceed the full margin of dumping (full margin of subsidy in the case of countervailing duties), and it is desirable that the duties be less than the margin, if such lesser duties are adequate to remove the injury.*109 Secondly, in regulating the provisional measures, the Code gives preference to the use of a security by cash deposit or bond than the use of provisional duties, whereas no such preference is provided in the Subsidy/Countervailing Duty Code.*110

(I) Antidumping on Behalf of A Third Country

One important feature of antidumping duties is that they can be used to prevent the domestic industry of a third exporting country from being injured by the dumped imports to the country imposing the duties.*111 It is however difficult to expect an importing country to impose antidumping duties for the benefit of a third country. If the importing country has no such industry of its own or its industry is not adversely affected by the dumped imports, it will certainly welcome the importation of such dumped imports which will in turn benefit its consumers or the industries using the imports as inputs.

(J) Committee on Antidumping Practices, and Consultation, Conciliation, and Dispute Settlement

The functions of the Committee on Antidumping Practices are the same as those of the Committee on Subsidies and Countermeasures, except that the Antidumping Committee is powerless to authorize countermeasures against misuse of antidumping duties and dumping practices.*112 Thus, the disciplinary power of the Committee on

Antidumping Practices is weaker than that of the Committee on Subsidies and Countermeasures. Since the Antidumping Committee cannot authorize countermeasures, a complaining party has to go to the Contracting Parties which has the ultimate power to authorize. Although the procedures of consultation, conciliation and dispute settlement provided in the Code are the same as those provided in the Subsidy/Countervailing Duty Code, the conditions for requesting consultation and thereafter conciliation and dispute settlement are different. The condition under the Subsidy/Countervailing Duty Code is the existence of an illegitimate subsidy and of nullification of benefits or of injury to the domestic industry of the complaining party.*113 Under the Antidumping Code, a party is entitled to request for consultation with another party or parties when it "considers that any benefit accruing to it, directly or indirectly, under this Agreement is being nullified or impaired, or that the achievement of any objective of the Agreement is being impeded, by another party or parties ..."*114 A party whose exports are subject to misuse or probable abuse of antidumping duties by an importing party would certainly have the right to request for consultation, and may obtain remedy under the dispute settlement scheme of Article XXIII of the General Agreement, if the consultation or conciliation fails to reach an acceptable solution. For an importing country, it would be unwise to seek remedy under the consultation, conciliation and dispute settlement scheme instead of using antidumping duties. This is because, on the one hand, the consultation, conciliation and dispute settlement scheme is less effective and slower than the use of antidumping duties. On the other hand, dumping is in many cases a private practice of a manufacturer without the involvement of his government, and the government may under domestic law have no power to prohibit the dumping practice. Thus, even though the Contracting Parties (rather than the Committee) has the power to discipline individual governments, its decision that the dumping practice should be eliminated may not be enforceable under domestic law. If the Contracting Parties authorizes countermeasures in the form other than antidumping duties such as withdrawal of concessions, it would be inappropriate for a government to be held responsibe for a private practice that it has no power to control. For a third country whose export interest is nullified by dumping, neither antidumping duties nor the consultation, conciliation and dispute settlement scheme can provide adequate remedy. As mentioned previously, it is difficult to expect that an importing country would impose antidumping duties on behalf of a third country, becase it would usually benefit nothing from, or even be adversely affected by, so doing.*115 If the third country seeks remedy under the dispute settlemnt scheme, the enforceability of th Contracting Parties' decision that the dumping practice in question should be eliminated may put the effectiveness of the remedy in doubt. Again it would be inappropriate if the decision is to authorize withdrawal of concessions.

An important question arising from the above quoted language is what the benefit accruing to parties under the Agreement and what the objective of the Agreement are. As noted before, the Code is intended to implement Article VI of the General Agreement. The purpose of Article VI is two-fold, i.e. to condemn dumping practices on the one hand and to impose control on the use of antidumping duties on the other hand. However, the emphasis of the Code seems to be on the control of antidumping practices rather than dumping practices. In its preamble, the Code recognizes that "antidumping practices should not constitute an unjustifiable impediment to international trade

..."*116 There is however no language to the same effect with regard to dumping. If the quoted language regarding the Code's jurisdiction is narrowly interpreted, benefits that are nullified by dumping will not be able to be remedied under the dispute settlement scheme of the Code. Instead, such a complaint shall be brought to the Contracting Parties which has a broad jusrisdiction as to cover all disputes concerning nullification of benefits under the General Agreement. When the complaint in issue relates to an antidumping practice rather than a dumping practice, it is unclear whether the parties should complete the dispute settlement procedures under the Code before they can avail themselves of the rights under the General Agreement. The remaining problem is whether the Contracting Parties will base its decision on the report of the investigating panel established by the Committee on Antidumping Practices, or it will appoint a new panel to have a de novo investigation.

Finally, the request for consultation or the request for the establishment of an investigating panel should be in writing.*117 In regard to the latter request, the written statement should contain such information as how a benefit under the Code has been nullified or impaired or how the achievement of the objective of the Code is being impeded.

Section III: Further Discussions on Dumping and Antidumping

(A) Cost of Production and Normal Value

Several national antidumping practices disqualify sales prices below cost of production as the basis for the determination of normal value. The most notable one is Sec.773(b) of the U.S. Tariff Act of 1930, as amended by the Trade Agreements Act of 1979, which reads as follows.

"... If the administrating authority determines that sales

> made at less than cost of production
> (1) have been made over an extended period of time and in substantial quantities, and
> (2) are not at prices which permit revocery of all costs within a reasonable period of time in the normal course of trade,
> such sales shall be disregarded in the determination of foreign market value ..."*118

When the remaining sales, which are not made at less than cost of production, are not adequate as a basis for the determination of normal value, constructed value shall be used.*119 The rationale behind such a rule is that sales below cost of production are not in the ordinary course of trade and therefore their prices would not fairly reflect the value of the products in question.*120 This rule, as applied by the Treasury Department in the Gilmore *121 case, is a clear rejection of the argument that sales below cost of production can be normal business practice in recession. Furthermore, this rule does not allow room for the case where there is not only cyclical but structural surplus capacity and it is impossible to recoup the fixed cost calculated on the basis of book value rather than actual economic value of the fixed assests.

The Code does not explicitly mention whether the rejection of sales below cost of production as a basis for the determination of normal value is in violation of the Code. One argument may be made to legitimize this practice. The Code, in allowing constructed value as an alternative of the export price for a third country in the determination of normal value, may assume that any normal value shall be above cost of production. This is because constructed value is composed of cost of production and other costs as well as a certain amount of profit. The issue of sales below cost of production is closely related to the problem of basic price system discussed below.

(B) Basic Price System

The basic price system has been variously employed by national governments in detecting dumping elements in imports. The actual operation of the system varies from country to country, but they all involve the establishment of a basic price for the application of either substantive or procedural rules of antidumping law, or even both. The legality of the basic price system as practiced by Sweden, the U.S. and the EEC is examined in the following.

(1) Swedish Practice *122

In 1954, the Swedish Government issued a decree which imposed antidumping duties on nylon stocking imports from Italy, whenever the invoice price was below the minimum price fixed by the Government. Importers were entitled to a refund if the case of dumping was not established. Later, the government made some changes in a new decree, according to which the basic price was no longer a factor in the determination of dumping and duties. Rather, it was used to exempt those sales made above the basic price from antidumping enquiries. As to other imports, the determination of dumping and the duties imposed was related to the concept of normal value stipulated in Article VI of the General Agreement. Despite the change of the nature of the basic price system, the Italian Government brought its complaint to the GATT claiming that the use of basic price as an administrative device was inconsistent with Article VI and other provisions of the General Agreement, and the administration of the system impaired benefits accruing to Italy under the General Agreement.

The Italian Government first contended that the basic price system as practiced by the Swedish Government discriminated against low-cost producers and deprived them of the competitive advantage to which they were entitled under the MFN clause. High-cost producers could escape antidumping duties even though their sales in the importing market were subsidized by high home market prices, so long as their export prices were not lower than the basic price. On the other hand, low-cost producers were subject to antidumping investigation, even if their sales in the importing market were not subsidized. The Panel in the present case ruled that Article VI did not oblige an importing country to impose antidumping duties on all imports sold at prices lower than normal value. Therefore, allowing high-cost producers free from antidumping duties was not inconsistent with Article VI. However, if the low-cost producers had been delayed or subject to uncertainties by the application of the basic price system, it would have a serious discriminatory effect.

Secondly, the Italian Government argued that the calculation of the basic price was unrelated to actual prices of various markets of exporting countries and therefore the system could not be reconciled with Article VI. The Panel was of the opinion that the system "would not necessarily be inconsistent with the provisions of Article VI so long as the basic price is equal to or lower than the actual price on the market of the lowest cost producer." (emphasis added)*123

The panel concluded the Swedish basic price system in regard to its legality with the following remarks:

> "(a) that the basic price system was not inconsistent with the most-favoured-nation clause or with the provisions of Article VI,
> (b) but that, in practice, the administration of that system might easily run into conflict with those obligations.
>
> Unless the customs authorities were prepared to decide on the alleged cases of dumping in a matter of days after arrival of the the consignment, and unless the basic prices were constantly kept under review to make sure that they did not exceed the actual prices prevailing for all varieties of stockings on the domestic markets of the most efficient producers, there was a certain danger of discrimination against low-cost producers in individual cases. Constant

> supervision of the operation of the scheme would also be necessary in order to avoid that it might be turned into a general protection against low-cost producers, even in the absence of dumping practices." (emphasis added)*124

Other References

Article 5 of the Antidumping Code provides that the initiation of an antidumping investigation is subject to the condition that there is sufficient evidenc of dumping, injury and a causal link. In the determination of whether to initiate an investigation, the evidence of dumping and injury shall be considered simultaneously. In Article 8 of the Code, the rule regarding the calculation and collection of antidumping duties under a basic price system is provided. An Understanding adopted in October 1981 by the Committee on Antidumping Practices in an attempt to clarify the confusion arising from Article 8 states that the rule is intended to facilitate the imposition of antidumping duties when several countries are involved.*125 The Article is not essential to the operation of the Code and should not provide a basis for opening an antidumping investigation or for the imposition and collection of antidumping duties. In other words, the rule is irrelevant in the discussion of the legality of using a basic price system as an instrument in antidumping administration. As regards using a basic price system as a monitoring device (like the TPM), the Understanding states that it was not

> "envisioned by either the GATT or the Antidumping Code. Nevertheless, these schemes can have the effect of burdening and distorting trade and could be used in a manner contrary to the spirit of the Code. Accordingly, the Committee agreed that such a scheme should not be used as a substitute for antidumping investigation and that their effects on international trade should be examined with a view,if necessary, to strengthening international discipline in this area."*126

The first part of the quotation indicates the inadequacy of existing rules regarding antidumping practices in dealing with the basic price systems as monitoring devices. The latter part discourages the use of the system as a substitute of antidumping investgation, but it does not mention the use of the system as an additional instrument rather than a substitute of antidumping investigation. It can also be inferred that in assessing the sufficiency of trade effects of a basic price system for the determination of legal liability regarding its use, lower criteria should be used so that a positive determination of liability can be more easily reached.

Using the guidelines established by the Panel in the present case and other guidelines discussed above, we shall examine the U.S Trigger Price Mechanism and the EEC basic price system under the Davignon Plan in the following.

(2) Trigger Price Mechanism (TPM) *127

In early 1978, the U.S. Treasury Department announced the Trigger Price Mechanism to be applied in antidumping administration regarding steel imports. The TPM is intended to provide a basis for initiating antidumping investigation without any prior complaint from the domestic industry. It is a device to monitor imports affecting the domestic industry viewed as a whole, rather than focusing on the investigation of individual complaints with respect to specific products. The trigger price is determined by using the unit cost of production in the most efficient exporting country, currently Japan, estimated at current prices and exchange rates. The costs of production cover traditional costs of labour, materials and directly related overhead, as well as general administrative expenses and a capital charge. The trigger price is reviewed and adjusted quarterly, and applies to all imports regardless of the source. It is constructed on a c.i.f. basis, i.e. transportation from Japan to each major importing region of the U.S. and the insurance costs are included in the trigger price. Importers are obliged to present a special summary steel invoice which must be certified that no rebates or unrelated incentives have been or will be paid in connection with the transaction. If the invoice price is below the trigger price, the information about the import concerned will be immediately forwarded to the Commerce Department for investigation. If warranted, a formal investigation will be initiated within a matter of weeks. After the completion of the Commerce Department's investigation, the case will be referred to the international Trade Commission for the determination of injury.

The TPM as described above is not intended to be a substitute of antidumping investigation. Rather, it concerns about the initiation of antidumping investigation. More importantly, it is not the determination of whether to initiate itself, but an additional device used to speed up the determination process. It is clear that the mechanism is used to single out imports that need further investigation as to whether formal investigation of dumping shall be initiated. It is however unclear whether the trigger price is also used in the determination process of whether to initiate an investigation as an indicator of sufficiency of evidence regarding the existence of dumping. If the trigger price is only used in the first case, there is no procedural rule prescribed in the Code that is applicable to the TPM, and the TPM in this sense is neither a legitimate nor an illegitimate practice. If the trigger price is also used in the second case, there is a problem of whether selling below the trigger price is a sufficient evidence of dumping. Although this is a decision to be made under the discretion of national administrating authorities, they should be able to prove those facts which can reasonably support their decisions in this regard, when faced with challenges.*128 The guidelines established in the Swedish Antidumping case may also be applicable to the issue of sufficiency of evidence, although it is primarily aimed at the relation of a basic price system to the MFN clause and Article VI under which no such requirement as to sufficient evidence of dumping in initiating an investigation is provided.*128

As regards the relation of the TPM to the MFN clause and Article VI, there is a problem of the applicability of the guidelines established in the Swedish Antidumping case. The basic price system as used by the Swedish Government was a device to exempt imports at prices higher than the basic price from antidumping investigation. Other imports would be subject to normal antidumping investigation. This is different from the function of the trigger price under the TPM, because the basic price was used in determining whether antidumping investigation should be initiated. Despite the difference in stages at which the trigger price and the basic price are used, their effects are the same. Once an import is confronted with the application of the trigger price or the basic price, there will be possible delay in consignment of the goods exported by low-cost producers who will also be subject to uncertainties. The only possible difference in effects is the time period during which the effects may last. There is therefore no reason why the guidelines of the Swedish case connot be applied to the TPM, as the guidelines are intended to minimize the effects. The adverse effects against low-cost producers were regarded by the Panel in the Swedish case as the element that may lead the use of a basic price system into conflict with the obligations under the MFN clause and Article VI, when there was no dumping found in the subsequent course of investigation. There is of course no problem of violating the MFN clause, if dumping is found to exist. As to the problem of exempting high-cost producers from antidumping investigation, there is no question of violating the MFN clause as Article VI does not oblige contracting parties to impose antidumping duties on all dumped imports.

If the Swedish case was applicable, the TPM would be faced with the following legal issues. First, to avoid being violative of the MFN clause and Article VI, the basic price shall not exceed the actual prices prevailing in the market of the most efficient producer. The trigger price is however based on the cost of production of the most efficient producer plus transportation and insurance costs. It is unclear whether in the Swedish case the Panel envisoned the possibility of selling below cost but above domestic market prices, or whether the Panel assumed that all market prices were above cost of production. If the Panel did envision the possibility and did not base its decision on that assumption, the TPM may well run into conflict with the MFN clause. Second, the customs authorities under a basic price system should be prepared to decide on the case in a matter of days after the arrival of the consignment, so that the delay and uncertainties would not become too serious. In the Swedish case, the Panel recommended 20 days. As the time needed to make a decision may vary from case to case, those cases that needs a longer time than a matter of days would be bound to conflict with the MFN clause. However, how long the effects last would constitute a violation of the MFN clause may also vary from case to case. Under the TPM, if the Commerce Department in determining whether to initiate an investigation tests the sufficiency of evidence in terms of the traditional price comparison, the trade effets that the TPM adds to those of a normal antidumping proceeding will end at the time the decision of whether to initiate an investigation is made. If in making the decision of whether to initiate an investigation, the Commerce Department uses sales below the trigger price as sufficient evidence of dumping and thereafter initiates an antidumping investigation, the additional effect will last and increase as the time goes on until at the earliest the preliminary determination regarding the existence of dumping is made. If the latter is the case, the TPM is very likely to violate the as-a-matter-of-days rule, as a formal investigation is to be initiated within a matter of weeks after the Commerce Department makes a decision based on the information forwarded to it.

Even though the Swedish Antidumping case is not applicable to the TPM, and the TPM is not considered as violative of the MFN clause, the TPM is still to face another challenge based on the non-violation nullification of benefits clause. The TPM like the Swedish basic price system would exempt high-cost producers from antidumping investigation. Therefore, high-cost producers are free to dump so long as they charge at prices higher than the trigger price. Allowing high-cost producers to be free from antidumping investigation is not violative of the MFN obligation as Article VI which is an exception to the MFN clause does not oblige an importing country to impose antidumping duties on all dumped imports. Low-cost producers are thus deprived of the price advantage. The change in the competitive relation of the exporters to the U.S. may nullify the benefit of MFN tariff concessions that low-cost producers gained in previous rounds of negotiation. In assessing the sufficiency of the trade effects for a case of non-violation nullification, lower criteria as suggested by the Understanding should be used.

(3) The EEC Basic Price System *129

As mentioned in Chapter III of Part One, the EEC basic price system is a part of the Davignon Plan which was designed to meet steel crisis in the Community. The basic price system was used by the Commission as a leverage to negotiate bilateral agreements with foreign producers to limit imports into the Community. The basic price system as applied by the EEC operates as follows.*130 The basic prices are determined "on the basis of their lowest normal value in the supplying country or countries where normal conditions of competition prevail." In practice, since sales prices below cost of production are not considered as prices under normal competition, the published basic prices are calculated by reference to the production costs in the country having the most efficient manufacturer. Under the system, all exporters to the EEC are required to complete an import license giving details of the prices of the product concerned. If the price of an import is lower than the relevant published price, a *prima facie* case of dumping is deemed to exist. The Commission will then be informed and subsequently either open an enquiry and impose a provisional duty or, in the case that there is an existing enquiry by a member state, impose a provisional duty. The provisional duty almost invariably corresponds to the differential between the import price as disclosed in the license and the published basic price. After the imposition of a provisional duty, full investigations will be initiated and the rights of the parties under the Antidumping Code will be respected.

Unlike the basic price system under the TPM, the EEC basic price system is used not only as a monitoring devise but also as a substitute of a part of the antidumping investigation, i.e. that part of the investgation which under normal circumstances an administrating authority has to go through in order to reach a preliminary determination of dumping and a determination regarding the sufficiency of evidence of injury. According to the Understanding cited previously. *131 such use of a basic price system should not be allowed. Although the use of a basic price system is said not to be envisioned by either the GATT or the Antidumping Code, there is still a possibility that the basic price system as applied by the EEC is in violation of the procedureal rule regarding the use of provisional measure and initiation of investigation. Article 5 of the Code stipulates that the initiation of an investigation by authorities is conditional on that there shall be sufficient evidence of dumping, injury and causation. Under the EEC basic price system, an inquiry can be opened without considering the sufficiency of evidence of injury and causation. There is also a problem of whether selling below the relevant basic price can be deemed as sufficient evidence of dumping.

Article 10 provides that provisional measures can be used only after a preliminary affirmative determination of dumping and sufficiency of evidence of injury. Under the EEC basic price system, provisional antidumping duties can be imposed upon the discovery of a sale at a price below the basic price. Again, the problem of sufficiency of evidence of injury aside, there is a problem of whether a preliminary affirmative determination of dumping can be reasonably reached when the basic price is the sole consideration.

Both problems of Article 8 and 10 are not serious ones for the EEC to overcome, as arguments can be made without much difficulty to justify the use of a basic price system in a determination on sufficiency of evidence of dumping and a preliminary determination of dumping. As to sufficiency of evidence of injury, current injury test as applied by national authorities are extremely low. Thus, it should not be difficult to demonstrate the sufficiency of evidence, and the EEC does not need much effort to make the operation of its basic price system consistent with the procedural rules of the Code.

Apart from the procedural rule, like in the case of TPM, the EEC basic price system is also faced with the problem of the MFN clause. Since the resulting effect of the EEC basic price system and the TPM are the same, the discussion on the legality of the TPM by reference to the Swedish Antidumping case should be applicable to the EEC case. The only difference, which would not affect the applicability, is the stage at which the basic price systems are applied and the resulting difference in the degree of damage which is related to the stage of application, especially the damage resulted from the imposition of provisional measures, suffered by those exporters who subsequently are found not practicing dumping.

The non-violation nullification of benefits clause is also applicable in challenging the EEC basic price system, if a claim based on the authority of the Swedish Antidumping case is not successful.

CONCLUSION

As most economists agree that an importing country, from an economic point of view, has little justification to act against foreign dumping, antidumping duty law is hardly an instrument for economic policies. Rather, it has become an instrument to ease social-political tensions resulting from trade. However, under the GATT system, social-political tensions resulting from trade are to be dealt with under the safeguard clause. What justifies an importing country to have an extra instrument which is easier to invoke? A common-sense explanation would be that dumping is an unfair trade practice and dumpers deserve less legal protection. Moreover, the notion of unfairness helps those affected by dumped imports to argue for a case of imbalance of interests among domestic sectors, and thus to increase the tension to a level which trade without dumping would not result in. The fundamental problem then is whether dumping is really unfair. What is the definition of "unfair"? The issue will be dealt with the concluding part of this thesis.

Footnotes (Part Two, Chapter IV)

1. J.Viner, 'Dumping: A Problem in International Trade', pp.24-29
2. B.S. Fisher, "The Antidumping Law of the United States: A Legal and Economic Analysis", 5 L & P in Int'l Bus., 1973, pp.85, 88-9
3. J.J. Barcelo, "Antidumping Laws As Barriers to Trade -- the United States and the International Antidumping Code", 57 Cornell L.R. (1972), pp.491,499
4. Viner, see note 1,pp.27-9
5. Fisher, see note 2, p.88
6. Barcelo, see note 3, p.502
7. Naturally, there may also be shortfall.
8. R. Dale, 'Antidumping Law in A Liberal Trade Order', p.172
9. P. Lloyd, 'Antidumping Actions and the GATT System', p.16
10. If devaluation is employed, although the export prices are thus lowered, the domestic prices of the exportables cannot reflect the true scarcity of foreign exchange and export receipts are lower than the true value. P. Lloyd, Ibid.
11. R. Dale, see note 8, pp. 35-6
12. Ibid.
13. P. Areeda and D. Turner, "Predatory Pricing and Related Practices under Section 2 of the Sherman Act", Harvard L.R. Feb. 1975
14. R. Dale, see note 8, p.24
15. J. Robinson,'Economics of Imperfect Competition', pp.201
16. R.Dale, see note 8, pp.38-9
17. P. Lloyd, see note 9, pp.13-4
18. R. Baldwin, 'Nontariff Distortions to International Trade', pp.142-3
19. Barcelo, see note 3, pp.503-4; Dale, see note 8, pp.36-7
20. Barcelo, see note 3, pp.506-7
21. Baecelo, see note 3, pp.508-13
22. Lloyd, see note 9, pp.13-4
23. Ibid
24. More on the liberal traders' proposal for legal reform will be discused in Part Three
25. BISD Vol. IV pp.10-2
26. Article 3:4 of the Code of 1979, BISD 26S/171
27. Article 4:1 (ii)
28. Article 5:1
29. Article 6:3
30. Article 10:3
31. Article 13
32. Preamble
33. Article 11 (iii) of the Code of 1967
34. Sec.772, Trade Agreements Act P.L. 96-39, 96th Congress
35. see Voss International Corp v. United States , C.D. 4801, 7 May 1979 as reported in Cust. Bull. Vol.13, No.13, 6 June 1979, pp.31
36. TAA Sec. 772(b)
37. TAA Aec. 772 (d) (1) (A)
38. TAA Sec. 772 (d) (2) (A)
39. TAA Sec. 772 (e) (1)
40. TAA Sec. 772 (e) (2)
41. Antidumping Act 1968-9,(hereafter the Canadian Act), Chapter 1, Article 10
42. Article 8(a), council regulation (EEC) No . 3017/79 of 20 December 1979, O.J. Vol. 22, L.239

43. Article 2:5 of the Antidumping Code, BISD 26S/171
44. Ibid
45. Supplementary Information, para. 11, Department Commerce's Regulations on International Trade Administration, (hereafter the Commerce's regulations), 19 CFR Part 353, Fed. Reg. Vol.45, No.26
46. Article 10:2(b), the Canadian Act, see note 41
47. Article 8(b), the Canadian Act, see note 42
48. Article 2:1 of the Code
49. Article 2:2 of the Code
50. ITC 1980, 2 ITRD 5458
51. TAA Sec. 771:15
52. Chr. Bjelland & Co. v. United States , 52 CCPA 178 (1972)
53. J.H.Cottman & Co. v. United States , 20 CCPA 344 (1932)
54. Animal Glue from the Netherlands , 42 Fed. Reg. 56829 (1977)
55. TAA Sec. 773 (a) (1)
56. Ibid
57. Article 9, the Canadian Act, see note 41
58. TAA Sec. 773(a)
59. Article 9, the Canadian Act, see note 41
60. TAA Sec 733(a)
61. Article 9, the Canadian Act, see note 41
62. TAA Sec.733(a); article 9 of the Canadian Act, see note 41
63. Article 2:3 of the Code
64. Ibid
65. Article 2:3 of the Code
66. Article 2:4 of the Code
67. s.353.7(c) of the Commerce's Regulations, see note 45
68. s.353.(d)
69. Ibid
70. Article 2:4 of the Code
71. s.353.8(2) of the Commerce's regulation, see note 45; The 8% minimum profit rate was challenged in the 1977 meeting of the Antidumping Committee by other representations. The U.S. representative in defending the practice argued that the 8% rate was the average profit rate of all the manufacturing industries in the U.S. This argument met with the counterargument that the Code specifically required that the reference market for the determination of profit be the home market of the country of origin. BISD 24S/17 para.10 It is noteworthy that the Code does not make the rule mandatory, because it only say the rule is a general rule.
72. s.353.8 (3) of the commerce's regulations
73. Article 2:6 of the Code
74. TAA Sec 772(d) (1) (B)
75. TAA Sec.772(d) (1) (C)
76. TAA Sec.772(d) (1) (D)
77. TAA Sec.772(d) (2) (B)
78. s. 353.6(a) (1)
79. TAA Sec.773(a) (4)(B); s.353.15 (a) of the Commerce's Regulations
80. Ibid
81. Acrylic Steel from Japan , 41 Fed.Reg. 17.948 (1976); Alphine Ski Bindings from Australia , 41 Fed.Reg. 22.609 (1976)
82. s. 353.15 (c) of the Commerce's Regulations
83. Motocycle from Japan , (Treasury Department 1978) 2 ITRD 5204; Portable Electric Typewriter from Japan (Commerce Dept. 19809 2 ITRD 5449; Countertop Microwave Ovens from Japan (Commerce Dept. 1980); Precipitated Barium Carbonate from Federal Republic of Germany

(Commerce Dept. 1981) 2 ITRD 5610
84. Notes, "Treasury Runs the Maze: Less Than Fair Value Determinations under the Antidumping Act of 1921", 8 Ga.J.of Int'l and Comp.L. (1978) pp.919,1036
85. TAA Sec. 773 (a) (4) (A)
86. Ibid; The 20% rule has been criticized as disregarding the fact that they are few sales either in the home market of the exporting country or to third countries can reach the same quantity levels as those sales to the United States.
87. s. 353.16 of the Commerce's Regulations
88. Ad. Article VI para.2, BISD Vol.IV, p.64
89. TAA Sec. 773 (c)
90. s. 353.8 (b) (1) of the Commerce's Regulations
91. s. 353.8 (b) (2)
92. Dale, see note 8, p.175
93. s. 353.8 (b) (3)
94. Article 9 (7) of the Canadian Act
95. Article 2:5 of the EEC Regulation, see note 42
96. TTA Sec. 773 (c)
97. Commerce Dept. 1981, 2 ITRD 5364; A so-called "market basket" test was suggest by Professor Anthony. His assumption is that the value of any goods in a free market is always a relative one, and must be measured in terms of the relationship that its price bears to the price of other goods. The test therefore is whether "in the circumstances of each case, state interference distorts the relationship that the (price selected under the normal test) would bear to other prices under a generally free market economic system". If the price ratio in the home market is roughly the same as those in free markets, the price selected under the normal test is a valid one for the purpose of measuring fair value. see R.A. Anthony, "The American Response to Dumping from Capitalist and Socialist Economies -- Substantive Premises, and Restructured Procedures after the 1967 GATT Code", 54 Cornell L. R. (1969) pp.159, 209
98. BISD 24S/17
99. G.A. Maciel, "International Framework for World Trade", Brazilian Proposals for GATT Reform
100. BISD 26S/171
101. BISD 26S/184
102. Decision of 5 May 1980 (ADP/2), Committee on Antidumping Practices BISD 27S/16
103. Ibid, BISD 27S/17
104. Ibid
105. see Part Two, Chap.I, Sec.II, (C) (1) (a)
106. see Part Two, Chap.I, Sec.II, (C) (2)
107. Ibid
108. Ibid
109. Article 8:1
110. Article 10:2
111. Article 12
112. Article 15
113. Article 15:2
116. BISD 26S/171
115. One exception is that the importing country has a bilateral arrangement with the third country to take such kind of antidumping action on a reciprocal basis.
114. Article 15:2

117. Ibid
118. TAA Sec. 773 (b)
119. Ibid
120. A Comprehensive Program for the Steel Industry , Report to the President by the Interagency Task Force, A. Solomon, Chairman; Implemetation of Trigger Price Mechanism by the U.S. Treasury (Jan.9, 1978)
121. see Carbon Steel Plate from Japan (the Gilmore case) 42 Fed. Reg. 194
122. Swedish Antidumping Duties , 2S/81
123. Ibid, pp 86
124. Ibid
125. Draft Understanding adopted on 26-27 Oct. 1981 -- Basic Price Systems and Special Monitoring Schemes
126. Ibid
127. For discussions on the use of the TPM by the U.S. in restricting foreign steel imports, see Part One, Chap.III
128. The requirement only appears in the Code
129. see the discussion in Part One, Chap.III on Steel Industry
130. Commission Statement Concerning Basic Prices of Certain Iron and Steel Products, O.J. Dec. 1977, No. L/353/1
131. see note 125

PART TWO

LAW OF SUBSIDIES, DUMPING AND MARKET SAFEGUARD

Chapter V

Safeguard Law

Chapter V : Safeguard Law

Section I: Safeguard in General

(A) Definition of Safeguard

The term "safeguard" when used in the context of international trade refers to the taking of action by the government or industries of an importing country to limit the inflows of foreign goods. When a safeguard action is taken by a government, it can be in the forms of import quotas, increased tariffs, or even a voluntary export restraint by an exporting country of the good concerned. Governmental action may be for the reasons of national security, public health and safety, the penetration of subsidized or dumped imports, supporting domestic agricultural policies, imbalance of payments, or relieving domestic producers from market disruption caused by a sudden surge in import competition. Private safeguard actions by industries, usually encouraged by their governments, are primarily aimed at the reduction of pressure from import competition. Private safeguard actions can be seen when a domestic industry tries to secure a commitment from foreign producers to reduce the volume of exports to the importing country. The concern of this chapter is focused on governmental emergency safeguard actions, that is, actions intended to relieve a domestic industry from a sudden surge in import competition.

(B) Economic Aspect of Emergency Safeguard Actions

The only efficiency case for safeguard action which can be made is that, being relieved from the surge in import competition temporarily, a domestic industry or firm would become equally or even more competitive than the foreign producers whose exports are subject to the safeguard measures. In some cases, this is achieved with the assistance from government subsidies to restructure the production pattern, such as replacing aging machines with more advanced ones. The surge in import competition may be due to the lowering of tariffs as a result of multilateral negotiations, changes in comparative advantages in the production of a specific product, or even changes in consumer tastes.

An economic case for safeguard actions can be more readily made by using the notion of externality, i.e. by using such broader concepts of social benefits and social costs. It is true that import competition can bring down the price of a specific product in the importing country which therefore gains from allowing the inflows of more competitive foreign products. Despite this gain, the importing country may suffer some damage from imports which is not fully calculated by the market. Such damage includes the cost of unemployment, the cost of transferring displaced resources to new activities, and the value of the output foregone until resources are transferred to new activities.*1 An emergency safeguard action can slow down the penetration of foreign imports and allow more time for adjusting to other activities, and thus reduce the dislocation costs. Nonetheless, there is also a cost involved in taking safeguard actions, including the administrative expenses and the loss of consumer gain from cheap imports.*2 The government of the importing country therefore has to decide whether the country has a net social benefit from imports, and at what point in time the marginal social damage from imports would exceed the marginal cost of import restriction. These decisions are to be made in the context of political economy and very much depend on the politics of individual nations. At a time of structural changes in the world economy and economic recession, the social cost of market readjustment tends to be higher, and usually politically over-valued.

As a result of taking a safeguard action by the importing country, there would be losses to the exporting country. The relevant question in this connection is which party, the importing or the exporting country, shall bear the cost of dislocation or of avoiding dislocation. The burden shall fall on the party which can be more efficiently minimize these costs. This question in turn relates to another question, i.e. whether the exporting country shall be compensated when its exports are subject to safeguard measures. One practical problem is, however, who shall decide on these questions, and how the decisions can be made. The only apparent case can be found is when the exporting country is a developing country and the importing country is a developed country. It is generally true that under such circumstances the importing country is better able to make a cost-benefit analysis and can more efficiently minimize the costs.*3 In this case, the importing country when imposing safeguard measures shall compensate the exporting country or <u>bribe</u> (rather than coerce) the exporting country not to export.*4 Other than practical difficulties, distribution of the costs of market readjustment in terms of efficiency, though theoretically sound, may not be acceptable to the countries concerned, especially the importing country which may feel strongly that it has a sovereign right to protect its market from disruption. Thus, the principle of reciprocity, which has little relevance to global efficiency but gives parties concerned a broad sense of justice, appears more favoured by trading nations in settling the issue of distribution of costs of trade. According to the principle of reciprocity, the importing country is to bear the costs, because the safeguard action may deprive the exporting country of the benefits which the exporting country has paid for by granting concessions to exports from the importing country. Hence, the exporting country shall be compensated for the benefits lost, or can take retaliatory measures against the importing country.

(C) Political Aspect of Emergency Safeguard Actions

Apart from the political elements in assessing the social cost that a country may suffer from market disruption, there are political considerations which make a safeguard system indispensable in trade liberalization. Without a safeguard clause, a government would find it difficult to persuade its domestic interest groups to accept an international agreement which would expose the domestic market to more foreign competition. From this prospective, a safeguard system may have positive contribution to trade liberalization. Conversely, if a safeguard system is too liberal or subject to abuse, it would frustrate the international agreement and the movement towards improved efficiency.

(D) Safeguard Instruments

Various policy instruments can be employed in a safeguard action: quotas, tariffs, and voluntary export restraints. There is also a substitute for safeguard action, namely, subsidies. The effects of these instruments are examined and compared from the standpoints of both the importing and the exporting countries.

It is apparent that the imposition of tariffs on a specific product would raise domestic prices, increase domestic production and decrease imports, and lead to a reduction in domestic consumption, of the product. Part of the loss in consumers' surplus goes to the government in the form of tariff revenue, and another part goes to domestic producers in the form of an increase in producers' surplus. The rest is the cost of imposing tariff to the society as a whole, which includes the cost of misallocation of resources in production and distortion in consumption. In the case of safeguard action, these costs reflect the costs of the action. The use of quota would have the same effects as that of tariff, except the tariff revenue in the latter case would go to the quota holders in the former case. It is possible for the government of the importing country to aution off the quota rights itself and gain a profit therefrom, but this would involve an extra administrating cost. If the government opts to distribute the quotas to importers by issuing import permits, it is those importers who will have windfall gains. In the case that the quota rights are distributed to foreign producers, the tariff revenue will go to the exporting country.

When being compared with quotas, tariffs are considered a better policy instrument from the importing country's point of view. First, as mentioned previously, under a tariff system the difference between the domestic and international prices of a commodity goes to the treasury of the importing country; whereas under a quota system the differential goes to private importers or foreign exporters as an unearned windfall. Second, if the quotas are distributed by import permits, new and rapidly growing domestic firms which import commodities to be used as inputs of production will be adversely affcted because import permits are usually allocated according to import shares that each firm held before the introduction of a quota system.*5 Third, under a tariff system, domestic final or intermediate consumers can still purchase more if they are willing to pay higher prices, whereas under a quota system they should consume at the level set by the government. Fourth, exporters of the importing country are also penalized by a quota system, because under a tariff system it can receive refunds of import duties on materials used as production inputs of the exported goods.*6 Moreover, the exporting country would also prefer a tariff system under which it can still increase its market share if its producer can lower their costs relative to those of the domestic producers or are willing to accept low profits.

Despite the advantages of using tariffs as a protective instrument, governments often prefer the use of quotas in safeguarding domestic markets. This is because a country, when faced with an inelastic supply of exports, would find it difficult to limit imports by using tariffs. A tariff system under such circumstances can only improve the terms of trade of the importing country, but would have little effect on the domestic price of the goods.*7 Domestic producers would thus be outcompeted. Moreover, a quota system in the case of downward shift of foreign supply curve can stabilize the circumstances of domestic production and the government does not need to adjust tariffs for every shift of the foreign supply curve.*8

An exporting country would prefer the use of voluntary export restraints to import tariffs or quotas imposed by the importing country to settle the issue of market disruption. Other than the fact that the price differential goes to the exporting country, an arrangement of VER would reduce the volume of sales to the importing country concerned, but increase the profit per unit. And under certain conditions which are not difficult to fulfill, the total profits will increase.*9 From the importing country's point of view, VERs are the most costly protective instruments.

(E) Alternative to Safeguard Action

Using subsidies to protect domestic markets is the first-best policy in the sense that it entails the least welfare loss to the importing country. Subsidies can be used to maintain employment of factors in the import competiting industry. There is welfare loss because the value of the marginal products of the factors in the industry is less than it would be, should they be employed elsewhere.*10 However, a large part of the subsidy is merely a transfer within the importing country, unlike in the case of quota where there may involve a transfer to the exporting country.*11 Moreover, such a subsidy does not result in any loss to consumers, while both tariffs and quotas do.*12

The welfare loss resulting from the use of a subsidy for the above purpose would not occur when subsidies are used in assisting factors to move out of the import competiting industry and to the new industries (adjustment assistance), or are paid directly to the factors regardless of whether they stay in the industry or not.*13 Despite the advantages of using subsidies to alleviate the social consequences of import competition, industries may still prefer to be sheltered behind the protection of tariffs or quotas, and the government may hesitate to use the subsidy approach because of the fiscal cost in its pursuit.

(F) Adjustment Assistance As A Complementary Instrument

A safeguard action can have the effect of slowing down the penetration of foreign competition and therefore gives more time for domestic import competiting industries to adjust to more efficient production pattern, or for the transferring of factors of production to more productive uses. On the other hand, adjustment assistance can accelerate the pace of absorption and digestion process that the importing country has to go through in order to eliminate the social consequence of slow digestion or absorption, or no digestion and absorption at all. Optimum policy would therefore require the joint use of these two instruments so that adjustment can be achieved within the shortest period of time and at the minimum dislocation and other costs.*14

Section II: Emergency Safeguard Law under the GATT System

(A) Article XIX of the General Agreement and the Draft Safeguard Code

(1) Introduction

Emergency safeguards are dealt with in Article XIX of the General Agreement, the main part of which reads as follows:*15

> "1.(a) If, as a result of unforeseen developments and of the effect of the obligation incurred by a contracting party under this Agreement, including tariff concessions, any product is being imported into the territory of that contracting party in such increased quantities and under such conditions as to cause or threaten serious injury to domestic producers in that territory of the like or directly competitive products, the contracting party shall be free, in respect of such product, and to the extent and for such time as necessary to prevent or remedy such injury, to suspend the obligation in whole or in part or withdraw or modify the concession."

A safeguard action is therefore subject to several conditions: (1) there shall be unforeseen developments after the exchange of concessions, (2) there shall be "such" increase in imports resulting from the effects of unforeseen developments and of obligations incurred under the General Agreement, (3) the increased imports cause or threaten to cause serious injury to the producers of the importing country, (4) suspension or withdrawal of concessions shall not exceed the extent as necessary to remedy the injury, and (5) the safeguard action shall be applied to the specific product in question only.

A safeguard action can also be taken by an importing country on behalf of a third country.*16 In the case where a preferential concession with respect to a specific product is granted to an exporting country by the importing country concerned, the importing country may on request of the exporting country take safeguard action against a third exporting country whose exports of the product to the importing country cause or threaten to cause serious injury to the domestic industry of the exporting country receiving the preferential concessions. Such a rule is applicable to developing countries who benefit from the generalized system of preference, customs unions, or two or more countries that have close economic ties and grant preferential treatments to each other. It is quite impossible for a developed country to take safeguard action on behalf of a developing country, as the developed country can benefit from competition between developing countries and other exporters. However, it is possible that within a customs union or between any two countries that have a close economic tie, such safeguard action will be taken on a reciprocal basis.

Before taking a safeguard action, the importing country is required to notify its intention to the Contracting Parties as far in advance as possible, and shall afford other countries having substantial interest as exporters of the product concerned an opportunity of consultation.*17 However, in critical circumstances, a safeguard action can be taken without prior consultation, if delay would cause damage which would be difficult to repair, on the condition that consultation shall be effected immediately after taking such action.*18 In the course of consultation, the parties may reach an arrangement of voluntary export restraint which they consider could serve better interest to both sides because the exporting country can be compensated by increased profitability and the importing country can be relieved from legal constraints imposed by Article XIX.

When consultation fails to produce a satisfactory solution, the importing country is free to take safeguard actions and the exporting country is free to retaliate against the safeguard action by suspending the application of concessions or other obligations to the trade of the importing country taking safeguard action, or in the case that safeguard action is taken on behalf of a third country, to the trade of the third country.*19 The retaliation is subject to the following conditions: (1) the retaliatory action shall be taken no later than 90 days after the safeguard action is taken, upon expiration of 30 days from the day on which the notice of suspension is received by the Contracting Parties, (2) the concessions or other obligations, the application of which is suspended, shall be substantially equivalent to those suspended by the exporting country taking safeguard action, and the suspension of which the Contracting Parties does not disagree.*20

When a safeguard action is taken without prior consultation with the exporting country and the action causes or threatens to cause serious injury to the producers of the product subject to the safeguard action in the exporting country, the exporting country is free to take retaliatory action to prevent or remedy the injury, without being subject to the time constraints, if the delay would cause damage difficult to repair.*21

(2) Conditions for Taking Safeguard Actions

(a) Unforeseen Development

It is interesting to analyze the notion of unforeseen development in the context of Article XIX by reference to the notion of non-violation nullification of benefits of Article XXIII. Article XIX can be regarded as a specific form of the non-violation nullification clause besides Article XXIII. Article XIX provides remedy for nullification of a specifically defined benefit, i.e. the guarantee that a contracting party would not be seriously injured when committing itself to trade liberalization without the precondition that there shall be violation of a specific rule of the General Agreement by another country. The non-violation nullification clause under Article XXIII is usually associated with an action concerning a specific provision of the General Agreement, such as the one on the use of subsidies, regardless of whether there is violation of the specific provision. In contrast, Article XIX safeguard actions are usually not associated with other provisions. As discussed in Chapter I of Part Two, a valid case of non-violation nullification would require three conditions: (1) benefits, (2) reasonable expectation, and (3) sufficient trade effects.*22 If one considers that a contracting party of the GATT would not suffer serious damage as a result of entering into the General Agreement is a benefit accruing to each party, unforeseen development is a notion similar to that of reasonable expectation, and the necessary trade effect of course should be serious.

The first and the only case at the GATT level where the issue of unforeseen development was discussed is the Hatters' Fur case.*23 In that case, the U.S. in an effort to justify its withdrawal of a tariff concession under Article XIX, argued that a style change which greatly favoured women's fur hats with nap or pile finishes and resulted in increases in imports was a development that the U.S. negotiators could not foresee. The Czchoslovak representative in the Working Party under which a consultation on the present case was conducted, argued that

> "the term "unforseen development" should be interpreted to mean developments occuring after the negotiation of the relevant tariff concession which it would not be reasonable to expect that the negotiators of the country making the concession could and should have foreseen at the time when the concession was negotiated."

The interpretation was agreed by other members of the Working Party except the U.S. The Czechoslocak representative, basing on this interpretation, continued to argue that it was universally known that fashions were subject to constant changes and the style changes in women's fur hats should not be deemed as an unforeseen development.

It is noteworthy that the latter part of the Czechoslovak argument was concentrated on the nature of the unforeseen development. The U.S., while admitting that the shift in fashions and its resulting increase in imports were within the negotiators' expectation, emphasized that it was the degree of the shift and its effects that were beyond their expectation. This argument was not specifically discussed by the Working Party, and the interpretation made by the Czechoslovak representative and agreed by members of the Working Party other than the U.S. did not make differentiation between the degree and the nature of a change. However, in the conclusion of the Working Party's report on the present case, members of the Working Party except the parties in dispute,i.e. the U.S. and Czechoslovakia, found no conclusive evidence that the U.S. action constituted a breach of the General Agreement. It may be inferred that the "dgree" argument was not objected by these members of the Working Party.

If an argument based on the degree rather than the nature of developments is acceptable, there is a need to examine the relation between unforeseen developments and "such" increase in imports as well as serious injury. According to the "degree" argument, a change in circumstances of trade, the degree and the effects of which are without the expectation of the negotiators of the importing country concerned, may qualify as an unforeseen development. Since the degree of a change in trade circumstances and its effects are almost invariably reflected on the change in trade patterns, the increase in imports to the importing country concerned is an important and sufficient, if not the only, indication of the degree of change in circumstances of trade and its effect. The follow-up question is to what extent an increase in imports can be regarded as sufficient for an "unforeseen development". The notion of increase in imports under Article XIX is in turn linked with the notion of serious injury. In other words, the crucial point for the purpose of Article XIX is whether the increase causes or threatens to cause serious injury rather than whether the increase exceed a certain limiting point. These inferences lead to the conclusion that the requirement of unforeseen development is redundant as an increase in imports which causes serious injury could sufficiently prove that the degree of a change in circumstances of trade and its effect are without the reasonable expectation of the negotiators. This conclusion of course is conditional on the acceptability of the "degree" argument.

Apart from the above "degree" analysis, the necessity of maintaining the requirement of unforeseen development is very much in doubt, when one applies the discussion in Chapter I(A) of Part Two on the necessity of requiring reasonable expectation to establish a case of non-violation nullification of benefits.*24 As mentioned previously, Article XIX in parallel with Article XXIII provides protection to a special benefit, i.e. the guarantee that contracting parties will not suffer serious injury in the process of trade liberlization. This benefit can be prevented from being nullified by maintaining tariffs or non-tariff import restrictions at certain levels. The assumption in negotiating reduction of these barriers is that the negotiators basing on their judgements on the future development of trade gave away concessions only when they were certain that the domestic industry concerned would not be seriously affected as a result. The forecast on trade in a specific product by the negotiators would be fully taken into account when negotiation is conducted on a product-by-product basis. However, when the negotiation concerns across-the-board tariff reductions or the reduction of non-tariff trade barriers, the development in trade circumstances of a specific product would not be fully taken into account. Rather, the emphasis is on the overall balance of economic gains and losses as a result of the negotiation. Even negotiators could foresee a development in trade in a specific product, they would not be able to remedy the situation by granting less concessions on the product concerned. Article XIX, therefore, becomes a mechanism that can be used to deal with this kind of sectoral deficiency of across-the-board and non-tariff negotiations. Since the underlying purpose of Article XIX is to provide a mechanism for those deficiencies that cannot be fully dealt with in trade negotiations in so far as serious injury is concerned, with the changes in the negotiation pattern and subject, the scope of Article XIX should not be limited to those deficiencies that could not be foreseen at the time of trade negotiation. Instead, it is essential to expand its scope to cover all deficiencies that could not be remedied in trade negotiations. The requirement of unforeseen development is removed from the Draft Safeguard Code produced at the Tokyo Round negotiations.※25

(b) "Such" Increase in Imports

A determination of injury is preconditioned that there shall be an increase in imports of the specific product in question. Article XIX does not specify the necessary level of increase to fulfill the requirement. In the Hatters' Fur case, the increased volume of imports was substantial and the increase was even more apparent in value terms. The adequacy of level of increase in this case was not chanllenged by other members, including the complaining country Czechoslovakia, of the Working Party. The EEC regulation requires "such <u>greatly</u> increased quantities..." (emphasis added) *26 Moreover, in the Notes on Drafting, Interpretation and Application of Articles of the General Agreement, it is stated that

> "the phrase "being imported...in such increased quantities" in paragraph 1(a) of Article XIX was intended to cover cases where imports may have increased relatively, as made clear in paragraph 1(a) of Article 40 of the Havana Charter." *27

In Article 40 of the Havana Charter,*28 the word "relatively" was inserted between "such" and "increased" so that Article 40, whose counterpart in the General Agreement is Article XIX, could apply in cases where imports had increased relatively to domestic production, even there was no absolute increase in imports. The Draft Code does not clarify this issue. However, under the present GATT design, relative increase in imports can still fulfill the requirement of increase in imports. The acceptance of the "relative" notion would naturally greatly increase the possibility of a positive determination of necessary increase in imports. When considering the notion of relative increase in imports in conjunction with the causation requirement, the U.S. Senate Finance Committee in its report on Trade Reform Act of 1974 took the view that unless imports were increasing absolutely, they cannot be a substantial cause of serious injury.*29

The most difficult problem in deciding whether there is an increase in imports is the determination of time frame in which "increase" is to be tested. Article XIX provides no guidance in this regard. The only possible reference is the notion of "previous representative period" used in the determination of "more than an equitable share of world export trade" in the context of subsidies on certain primary products.*30 Previous representative periods as prescribed in the Subsidy/Countervailing Duty Code is normally the three most recent calendar years in which normal market conditions exist. The condition that there shall exist normal market condition is presumably applicable for the purpose of Article XIX, but whether three years are sufficient remains to be clarified.*31 This issue of selecting the time frame for the purpose of Article XIX was explored in detailed in a U.S. escape clause case, Stainless Steel and Alloy Tool Steel of 1976.*32 In that case, Commissioners of the U.S. International Trade Commission were at variance in regard to the determination of the time frame. Commissioner George Moore and Commissioner Catherin Bedell used the period between 1964 and 1975, in which imports of the products concerned were found to be in an increasing trend. The reason for using this time frame is to avoid a determination solely based on the period of 1968-74, during which there existed unusual market conditions, including a world-wide nickel strike and two recessions, and governmental action such as domestic price controls and voluntary restraint agreements with foreign producers. Contrary to the majority view mentioned above, Commissioner Daniel Minchew held the view that, in the absence of extraordinary circumstances, the Commission should look at the increase in imports resulting only from the most recent trade concessions, which in the present case were the trade concessions made at the Kennedy Round negotiations of 1967. By excluding those years before 1968, the injury considered would be a new and continuing injury from increased imports as opposed to an old injury. Those unusual conditions and governmental actions, in his view, did not warrant his looking beyond 1968. In his concurring opinion with Commissioner Michew, Commissioner Italo H. Ablondi explained further that those factors, argued by Commissioner Moor and Commissioner Bedell to be distortive, were neither unique to the subject industry nor so pervasive as to substantially distort market conditions.*33 He then, basing on the previous practice of the Commission, i.e. "to analyze imports over a period of time of sufficient length to establish trends and thereby put aberrant or temporary conditions into proper perspective", chose 1970 as the starting point because generally the period of time selected by the Commission has been 5 years.

The Stainless Steel case raises a couple of interesting questions. First, whether the determination of increase in import should be made by reference to the most recent concessions or all the previous as well as current concessions. Article XIX is not explicit on this issue. A relevant question is whether the injury to be protected is current injury or injury which has cumulated since the earliest concession was made. Commissioner Ablondi argued that it is the former that is to be protected by the statute because he found the language of section 201 (b) (1) of the Trade Act of 1974, which is the counterpart of Article XIX in the U.S. implementing legislation, was in present tense.

> "By using the present tense, Congress clearly intended that the Commission consider only imports which have occured during a period relative to the alleged injury. The Act requires that imports be related to the injury claimed, and that injury be current, or "new" injury. The relevant period of importation, then, must necessarily be close to the time of injury (that is, to the present time) rather than during earliest periods of importation having little or no impact on present industry conditions."

Such an argument conforms with the spirit of Article XIX. Contracting parties upon assuming GATT obligations or granting concessions to other parties in each round of negotiation would be presumed to adjust its domestic industry to the new trading conditions created by those obligations and concessions. Article XIX only provides temporary remedy for those countries which failed to adjust at the same speed as the development of market conditions. By taking safeguard action, the external changes in trading conditions can be prevented from taking full effect or from taking effect at full speed, and therefore domestic industry can have more time to adjust. The adjustment process is presumed to have completed or the industry concerned is not in a state of depression by the time next round of negotiations on the same product starts. Otherwise, the country concerned would not allow further concessions to be given away and exclude the product from the negotiation list.*34 Therefore, when one considers the problem of increased imports by reference to the occurrence of serious injury, the only time period which is of importance is the time after the conclusion of a new round of negotiation.*35 If imports following the conclusion of a new round of negotiation do not increase, there is certainly no injury to the industry concerned that is attributable to imports, and old injury, if there exists any, would not be a significant concern. Moreover, in the <u>Hatters' Fur</u> case, the Working Party emphasized that "action under Article XIX is essentially of an emergency character and should be of limited duration." The word "emergency" implies that Article XIX is intended to remedy the sudden occurrence of injury and old injury can hardly be said to occur suddenly.

The second question raised by the <u>Stainless Steel</u> case is when extraordinary circumstances exist. In the majority view of that case, the existence of a world-wide nickel strike, two recessions, domestic price controls, dollar devaluation, voluntary restraint agreements and antidumping actions against certain import was said to be sufficient for a case of extraordinary circumstances. However, the minority took a different view. Commissioner Ablondi explained that dmestic price controls, dollar devaluation, and recession were national in scope and not confined to steel industry; the nickel strike was temporary which only delayed imports until the following year; antidumping action only affected one product from one exporting country; and although VRAs affected imports, their impacts were subject to several factors including the voluntary nature of VRAs,*36 and the fact that a substantial number of exporters were not parties to the agreements. In short, according to Commissioner Ablondi, factors that make market conditions extraordinary should be specific to the industry concerned but general enough to cover the whole industry (or presumably at least a substantial part of the industry), and their effects should be substantial in degree.

Commissioner Ablondi was right in arguing that factors which affect market conditions on a national scale should not be considered as elements of extraordinary circumstances for the purpose of the escape clause action. When one applies previous analysis of the effects of a change in a general tax system to the present discussion of nation-wide factors, a factor which causes changes in production and trade of every product within a country should not be considered as a distortive factor. Since the market is not distorted by such a factor, it is still an ordinary or normal market, although there are changes in the volumes of imports. Such non-distortive factor is only relevant in determining whether and to what extent a change in imports is caused by a specific factor as required by law.

It is unnecessary to consider a world-wide recession as an element of extraordinary circumstances because it not only affects the volume of imports but also the sales volume of domestic producers. This means a world-wide recession would not affect the relative competitive positions of foreign and domestic producers. Even if a world-wide recession affects the relative trade position, the notion of relative increase can be used to remedy the situation. Moreover, undermining a period of time because it coincides with a recessionary period is unnecessary under some national legislation which requires the increased import as a cause of serious injury be weighed against other causes. It is very likely that recession under current state of economy is an important and even more important than increased imports as a cause of the deterioration of domestic industry. Therefore, under such escape clause law like that of the U.S. which requires weighing of each cause and the increased import be a cause no less important than others, a sufficient causation between increased imports and serious injury may be difficult to establish.

Finally, from the viewpoint of a country taking antidumping action, dumping is not an ordinary market condition and therefore a countermeasure like antidumping duties should not be considered as an extraordinary condition in so far as the same country taking safeguard action is concerned. On the contrary, a VRA is not an ordinary market condition because for the country taking safeguard action, it is a distortive rather than offsetting measure.

(c) Causation: Increased Import, and Unforeseen Developmnts and Concessions

According to the "degree" argument, the degree of increase in imports itself could constitute an unforeseen development. Hence, there is certainly no need to search for the causal link. Moreover, unforesen developments are no longer a significant precondition, after the change from product-by-product to across-the-board and non-tariff negotiations.

There is however still a need to establish a causal link between increased imports and the concessions that had been granted to trading partners. Article XIX does not specify the necessary causal link. It is conceivable that every increase in imports would have a acusal link of some degree to the concessions granted to other countries, or to trade obligations that the importing country assumes under the GATT. For instance, if the importing country was free to impose import quotas without regard to the prohibition of Article XI on the use of quota, imports would never increase. However, the case will be different, if the concession or benefit of Article XIX are meant to be those reached in the latest round of negotiation. The U.S. escape clause law in the 1950s required that the causation be "in whole or in part", and in the 1960s the requirement was changed to "in major part", and after the Trade Act of 1974, the requirement was removed amid easing conditions for its application. The same development can be seen in the Draft Code which does not condition a safeguard action on that an increase in imports should be caused by granting concessions to trading partners.*37

(d) Serious Injury

The only source at the GATT level that one can draw references from in respect of serious injury is the Hatters' Fur case. In that case the Working Party gave some general guidelines for the determination of whether conditions have been met for the use of a safeguard action. The Working Party first discussed the difference in appraisal of facts in terms of Article XIX by an importing country intending to take or having taken a safeguard action and other countries participating in an international body, such as the Working Party, under which a safeguard action is examined. While the importing country would naturally give more weight to its domestic factors, other countries would emphasize international factors and the interest of the exporting countries concerned. To reconcile these conflicting approaches, the Working Party stated that

> "..., it must be recognized that any view on such a matter must be to some extent a matter of economic judgement and that it is natural that governments should on occasion be greatly influenced by social factors, such as local employment problems. It would not be proper to regard the consequent withdrawal of a concession is *ipso facto* contrary to Article XIX unless the weight attached by the government concerned to such factors was clearly unreasonable." *38

Thus, to the extent that is not clearly unreasonable, an importing country is allowed to add social consideration into its economic judgement in appraising the seiousness of injury.

For the determination of injury, the Draft Safeguard Code gives some guidelines. The determination shall "be based on examination of *objective* factors having a bearing on the state of the domestic producers, such as: "(development and prospects with regard to) output, turnover, inventories, market share, profits, domestic prices, exports, domestic employment and wages, utilization of productive capacity, productivity, and investment (, as well as the size of the market)".*39 Presumably these objective factors only provide a basis for economic judgements and are subject to further appraisals which may involve a government's subjective view on the seriousness of injury suffered by a domestic industry. The Draft Code also provides a flooring rule which can be interpreted as setting the limit on a government's discretion empowered by the "clearly unreasonable" rule of the <u>Hatters' Fur</u> case. It is provided in Chapter 1 paragraph 1 of the Draft Code that no positive determination of the existence of serious injury can be made if those above-mentioned factors are not adverse.

In terms of quantum, it is commonly understood that serious injury is a standard higher than material injury. How far the quanta of these two injury standards differ from each other would vary with national practices. In the <u>Hatters' Fur</u> case, injury of substantial degree was regarded as sufficient by the U.S. to warrant a safeguard action, and this practice was not objected by the Working Party.*40 The U.S. Trade Act of 1974 requires that to establish a case of serious injury, the injury should be substantial in degree.*41 As to the nature of injury, there is a tendency to examine injury in the context of emergency safeguard from the prospective of an industry's future conditions. The U.S. ITC once held that serious injury should be "an important, crippling, or mortal injury; one having permanent or lasting consequence".*42 The ITC would uaually discount transitory factors in the evaluation of seriousness of an injury.*43 The same development can be seen in the Draft Code where the list of factors to be considered in the determination of serious injury is preceded by the bracketed language "development and prospect".*44

(e) <u>Threat of Serious Injury</u>

The Draft Code provides that a determination of threat of serious injury can be made only when serious injury, although not yet existing, is clearly imminent.*45 The same language appeared in the U.S. Ways and Means Committee Report on the Trade Act of 1974.*46 In the <u>Stainless Steel</u> case, the majority of the Commission based its positive determination of threat of serious injury on three facts: (1) a strong upward trend in imports, (2) the level of inventory in the hands of importers is three times the average level of previous three years, and (3) a large amount of unused capacity in foreign steel mills as well as large investment underway in new production capacity.*47

(f) Like or Directly Competitive Product (Industry)

The term "like product " is defined as a product which is identical in all respects with the imported product in question and, in the absence of such a product, a product which has characteristics closely resembling those of the imported product in the Antidumping and Subsidy/Countrervailing Duty Codes.*48 It is specifically stated in both codes that this definition only applies to the two codes.*49 Article XIX gives no definition in this regard, nor does the Draft Code. In the Australia Subsidy on Ammonium Sulphate case,*50 the Panel found that, for the purpose of Article III of the General Agreement which concerns non-discriminatory tax treatment and import charges, two fertilizers were not like products because according to the common tariff practice of trading nations these two fertilizers were listed seperately and enjoyed different treatments. In the Norwegien Sardin case,*51 the Panel though, for purpose of Article I (MFN) and Article VIII (non-discrimination of Fees and Formalities), it unnecessary to define the term "like product ". The crucial issue, according to the Panel, was whether in the negotiations of tariff concessions both parties in dispute expressly or tacitly agreed to treat those two products in question as if they were like products . In the EEC Measures on Animal Feed Protein case,*52 the Panel found that the products concerned were not like products because of such factors as "bindings, the varying protein contents" and different origin of protein products.*53 In sum, common tariff practices, the intention of the parties concerned at the time of negotiations, and product contents can all be used to decide whether products in dispute are like products. In addition, the term "like product " was defined by the League of Nations as a "practically identical" product. *54 The above mentioned criteria of course are not the only ones that can be used, and criteria may vary from case to case. However, the criteria used in the above mentioned cases are all less restrictive than the one used in the Antidumping and the Subsidy/Countervailing Duty Codes, i.e. identical in all respects.

With regard to the term "directly competitive product ", no definition is given in Article XIX or the Draft Code. In the EEC-Measures on Animal Feed Proteins case,*55 the Panel found that the products in dispute were directly competitive products because the effects of the EEC's security deposit scheme was to make Communities produced denatured skimmed milk powder competitive with imported vegetable proteins. Thus, the Panel at the present case looked to the effects of a practice in order to determine whether two products are directly competitive.

As to national practices, the U.S. ITC has made a series of rulings in this regard. The word "like" is said to relate to physical identity, while "directly competitive" has more to do with the notion of commercial interchangeability.*56 For instance, fresh mushrooms could not be considered as like products of canned mushrooms, while the two are considered as directly competitive products.*57 Component parts producers could not be proper petitioners for safeguard actions because component parts are neither like products nor directly competitive products of finished products.*58 Since "like" and "directly competitive" are connected by "or" and since the two were not intended to be synonymous or explainatory of each other, safeguard action can be invoked when either type of producers satisfies statutory requirements of injury.*59 When producers of "like products" can be clearly distinguished from producers of "directly competitive products", and the distinguishment is consistent with practices in marketplace, the ITC is to look to the group of producers which presents the most compelling argument for relief and use the group as the basis for safeguard action.*60

Producers (Industry)

The Draft Code contains a provision that the imports concerned shall cause serioud injury to a major part of all of the producers of the like or directly competitive products.*61 The Code also provides an alternative rule to the "major part" rule, that domestic producers refer to the domestic producers as a whole or to those whose collective output of the product constitutes a major proportion of the total domestic production.*62 No rules are provided for market segmentation and for imports by domestic producers. The U.S. ITC practice is that imports by domestic producers are counted in the determination of increase in imports, but not in the determination of serious injury.*63

(g) Causation: Increased Imports and Serious Injury

In regard to the causation requirement, Article XIX does not specify the necessary intensity of causation between the increase in import and serious injury. The language that "...such increased quantities ...as to cause or threaten serious injury..." can be interpreted as the increased import should be the only cause of injury in one extreme, and a cause of serious injury in the other extreme. No clarification at the GATT level on this issue has been made. In the negotiation of the Draft Code, a proposal was made to change the language of the causation requirement to "...such quantities ...demonstrably as to account for the principal cause of serious injury..."*64 The term "principal cause" was used in the International Antidumping Code of 1967 and had veen variously interpreted.*65

At the national level, the U.S. escape clause law in the 1950s required that "increased imports ... shall be considered as the cause (of injury)...when the Commission finds that (they) have contributed substantially towards causing or threatening serious injury to such industry."*66 (emphasis added) The quoted language can be read as that the U.S. interpreted the causation requirement of Article XIX as the only-cause requirement and the requirement can be fulfilled when in effect the increase in imports is only a substantial cause of the serious injury. In the 1960s the requirement was changed to that the increased imports "have been a major factor" in causing injury.*67 The interpretation of the term "in major part" in the Pianos and Parts case of 1969 was regarded as an equivalent of the question of whether " the serious injury would not be threatened if it were not for the increased imports." This is an application of the "but for" test established in the Eyeglass Frame case. *68 The Trade Act of 1974 changed the requirement to "a substantial cause of serious injury or threat thereof".*69 The term "substantial cause" is defined as "a cause which is important and not less than any other cause".*70 In the Stainless Steel case, it was stated that

> "where increased imports are just one of many causes of equal weight, it would be unlikely that they would constitute an "important cause", but where imports are one of two factors of equal weight, they would constitute an "important cause"." *71

The weighing of one cause against another makes it particularly important whether several factors can be considered together as a cause or they should be considered seperately as individual causes, when it is possible to put these factors together under a concret concept. The most notable instance of this kind is the relation between the concept of recession and those factors, the existence of which is an indication of the existence of recession. This is the central issue of the famous U.S. case Certain Motor Vehicles and Certain Chassis and Bodies *72 in which the majority of the ITC took the position that an escape clause action was not warranted, because imports, although an important cause, were not a cause not less than recession as a single cause. The main argument made to support treating recession as a single cause is as follows. Recession is not comprised of a simple aggregation of factors but rather a complex interaction of several factors. To single out any of the factors as a cause would fail to assess realistically the dynamics of the marketplace. The minority held the view that the congressional intent was to require the Commission to examine an industry over the course of its entire business cycle including both good and recessionary years. Therefore, adverse economic factors could not be aggregated and considered as a seperate cause. Otherwise, in a recessionary time, it would not be likely that a positive determination of causation would be rendered, regardless of the level of import penetration.

The majority view in the present case was consistent with previous practices of the ITC. In the Unalloyed, Unwrought Zine case,*73 the Commission held that the decline in demand for zinc, which was caused by a number of interdependent factors, was a more important cause of injury than increased imports to domestic industry. In the Bolt, Nuts, and Screws of Iron or Steel case,*74 Commissioner Moore found that the general condition of the economy was a cause more important than imports.

The threshold question in the above cases in regard to the definition of a cause seems to be whether those component factors can be seperated and the seperability depends on the intensity of interdependence between them. Such definition process would involve highly sophisticated econometrical and legal techiques. One way to avoid this complication is to list all the possible independent causes in the international agreement. In the Draft Code, a list of independent causes is given, which includes competition among domestic producers, contraction in demand due to substitution by other products or to changes in consumer tastes, decline in domestic consumption, shift in technology, structural deficiencies and loss of comparative advantage.*75 The list is of course not exhaustive.

(3) Domestic Procedures

The Draft Code provides the necessary domestic procedures that a national authority has to go through before imposing a safeguard measure on imports. No safeguard measures may be applied unless there is an examination as to whether those substantive conditions discussed previously have been met.*76 The procedures are similar to those in antidumping and countervailing duties administration. The initiation of a safeguard investigating proceeding is preconditioned by the requirement of evidence of serious injury.*77 The authority shall give public notices, allow participation by interested parties, protect confidential information and notify all interested parties including the exporting parties of the General Agreement concerned the result of the investigation.*78 There is also an important proposal in the Draft Code which suggests that no safeguard investigation be made with respect to the same subject matter as a previous investigation unless certain time has elapsed since the conclusion of the previous investigation.*79

(4) Use of Safeguard Measures

Use of safeguard measures, according to Article XIX, shall not exceed the necessary extent. The Draft Code makes the "necessary" standard more concret and requires that safeguard measures shall be proportionate to the injury.*80 The word "proportionate" is further substantiated by rules which stipulate the product coverage, the duration, and the terms for extention in the application of safeguard measures.*81 There are also rules designed to protect the interest of the exporting contracting parties whose exports are subject to a safeguard measure. Safeguard measures shall be progressively liberalized in order to encourage the adjustment of domestic producers to import competition, and they shall not reduce the level of imports below the level in a or the most recent representative period.*82 These rules may be softened to some extent depending on the result of future negotiations. There is also a proposal suggesting that no safeguard measures be applied by developed countries with respect to any product which was subject to a safeguard measure within the preceeding two years.*83

(5) Notification, Consultation, and Dispute Settlement

The Draft Code proposes several rules on such issues as the particulars and details that should be included in the notification of intention to implement a safeguard measure to the Committee on Safeguard Measures and in the notice to the exporting countries with a view to having a consultation with them.*84 The party implementing a safeguard action is also required to provide a supplementary notice to the Committee on Safeguard Measures giving full details of the safeguard action being taken.*85 The dispute settlement procedures stipulated in the Draft Code are similar to those for antidumping and subsidy/countervailing duty cases, but it is very likely that the Code's procedures will be subject to a great deal of modification, depending on how far the Committee on Safeguard Measures is allowed to exercise discipline on signatories.

(6) Committee on Safeguard Measures

The most important function of the Committee as provided in the Draft Code is to exercise surveillance on the use of safeguard measures. The Committee shall examine any safeguard measures, and any situation where a party's trade interest is likely to be affected because another party is not meeting its obligation under the Code.*86 The Committee may conduct such examinations, only on request of a party adversely affected by a safeguard measure or non-compliance of another party. There is, however, a proposal to enable the Committee to conduct examination without specific initiative from affected parties.*87 In its annual reports to the Committee, the party maintaining a safeguard measure shall explain to the Committee why it is necessary to maintain the measure and what progress is being made towards its removal, and the Committee shall conduct annual review on these reports.*88 The Committee's jurisdiction in regard to dispute settlement is similar to that of the Committee of Antidumping

Practices.*89 Most importantly, the Committee, though may disapprove or make recommendation regarding a safeguard measure, is powerless to authorize sanction against violation or non-violation nullification or impairment.*90 Such cases shall therefore be referred to the Contracting Parties which under the authority of Article XXIII can authorize counteractions. As to in what way Article XXIII might be resorted to, there shall be further negotiations.*91 It is noteworthy in this juncture that the right to retaliate against a safeguard measure is not subject to the authorization either from the Committee or from the Contracting Parties.

(7) Retaliation against A Safeguard Action

Once a safeguard action is taken, the balance of economic advantages between the exporting countries and the invoking country achieved in previous negotiations will be frustrated. Thus, there is a need, for the sake of reciprocity, to adjust the concessions that the exporting countries granted to the invoking country. Since it is the exporting countries which are adveresly affected by the safeguard action, they should have the discrection as to whether to adjust the concessions. This means they have the "right" to retaliate. An exporting country's right to retaliate against a safeguard measure is subject to certain degree of constraint under the Draft Code. When a safeguard measure, as agreed by an exporting country, has met the requirement of the Draft Code, the exporting country shall (or should normally or may) refrain from exercising its right.*92 The alternative language of "shall", "should normally", and "may" indicates the degree of constraint that may be imposed on the exporting country. A proposal intending to protect the interest of developing countries suggests that compensation shall be made to developing countries and they in turn shall refrain from exercising the right to retaliate.*93 Another proposal with a view to loosening the restriction that the right to retaliate shall be exercised within 90 days after a safeguard action is taken, suggests that the exporting country, when considering that the action had a serious adverse effects on its trade interest, be free to exercise its right to retaliate, notwithstanding the restriction.*94

(8) Non-discriminatory Application of Safeguard Measures

Unlike antidumping and countervailing duty actions, safeguard actions are not exempted from the general obligation of the most-favored-nation treatment. This means safeguard measures should be applied to all imports of a specific product concerned regardless of their origins. The rationale underlying such an application of the principle is that because of practicing dumping or receiving subsidies from their governments, foreign producers waive the protection of the MFN clause. However, in the case of safeguard action, producers in the exporting countries did not commit any "wrong" and therefore are still entitled to the MFN treatment. This requirement of non-discrimination together with the right to retaliate constitutes the most effective deterrent to the invocation of Article XIX. They are also effective safeguards of the export interests of developing countries which are less powerful in exerting political pressures to protect their economic interests and whose status as new entrants in the marketplace may make them emotionally identified as the source of increases in imports and therefore of market disruption. Some developed countries, notably the EEC countries, are fighting hard for the removal of the MFN restriction. One commentator also suggested that the principle of MFN and the right to retaliate are too effective as a derterrent to the invocation of Article XIX to encourage contracting parties to act within the legal framework of Article XIX.*95 Seeking safeguards outside the framework of Article XIX is usually in the form of voluntary export restraints or under the Multifiber Arrangement in the case of textile trade.

(B) Voluntary Export Restraints (VERs)

A voluntary export restraint is an act by an exporting country or private exporters to restrain its exports to other countries voluntarily. The use of VERs has a long history and has been in various forms. An arrangement of VER can be seen in international commodity agreements fixing export quotas for participating parties, in the administration of antidumping and countervailing duties when VERs are used as substitutes of the duties, in those national safeguard schemes which embody VERs as an alternative safeguard measure such as the orderly marketing arrangement (OMA) under the U.S. trade legislations, in bilateral agreements between governments intended to maintain balance of trade, or in private agreements between industries of the exporting and of the importing countries. Though different in form, all VERs have the effects of restricting trade flows and are therefore contrary to the spirit of GATT law. However, some VERs are legitimate under the GATT, such as the use of VERs as substitutes of antidumping or countervailing duties when necessary conditions are fulfilled. Other uses of VERs may run in conflict with Article XI of the General Agreement which prohibits the imposition of any import or export restrictions,*96 except when a VER arrangement is between private parties.

The threshold question in regard to the legality of those VERs not associated with a legitimate import control scheme is the extent of government involvement in the negotiation and conclusion of a VER agreement. Governmental involvements range from actual participation in the negotiation, provision of technical assistance to domestic producers, such as supervisions by government experts in negotiation, to granting immunities from domestic antitrust law to both parties of a VER agreement. Since most of the VER agreements are negotiated secretly and governments usually avoide being directly involved in the negotiation, it is difficult to find out the intensity of governmental involvement. Even if it is possible to find out the intensity of government involvement, the existing GATT rules provide no guidance as to what extent a government should be considered responsible for actions by its nationals.

A possible case can be made against an importing country or an exporting country which is a party to a VER arrangement is a case of non-violation nullification of benefits. Government involvement, no matter how slight in degree, can be regarded as an act which nullifies the benefits accruing to other contracting parties under Article XI. This is true even the act itself is not equivalent to an export or import restraint. The act contributes to the formation of an arrangement which has the effect of nullifying the benefits accruing to other contracting parties than the parties to the arrangement under Article XI. Thus, granting an antitrust immunity to an arrangement of VER can be considered as an act which nullifies the benefits of other contracting parties.

As to the private aspect of a VER, one way to control its use is through the antitrust legislation of each country. The feasibility of such an approach would depend on the power of the consumer unions in preventing national governments from granting immunities to VER agreements. Another approach of controlling the use of VER is through international cooperation to eliminate restrictive business practices in international trade, such as the Restrictive Business Practices Code approved by the UN Conference on Restrictive Business Practices.*97

(C) Multifiber Arrangement (MFA)

The Multifiber Arrangement presents a sectoral safeguard system which was incorporated into the GATT system as an exception to the general rules of the GATT, such as the MFN principle. The safeguard system as established under the MFA has some of the characteristics of Article XIX and legitimizes the use of VERs. Except its less stringent conditions for the invocation of its safeguard provisions, the MFA is more of an ideal safeguard design than Article XIX. Indeed, in many respects, the Draft Code adopts the design of the MFA, such as progressive liberalization of import restrictions.

Article 3 of the MFA sets out the conditions for taking safeguard actions against textile imports.*98 The most important condition is that there shall be market disruption in the importing country which intends to take safeguard action.*99 The indicia of market disruption are the same as those of serious injury in the context of Article XIX.*100 Moreover, the determination of market disruption must be based on the existence of serious damage to domestic producers or actual threat thereof.*101 It is also provided in Article 3 that "(t)he factors causing market disruption...and which generally appear in combination are as follows:

> (i) a sharp and substantial increase or imminent increase of imports of particular products from particular sources. Such an imminent increase shall be a measurable one and shall not be determined to exist on the basis of allegation, conjecture or mere possibility arising, for example, from the existence of production capacity in the exporting

> countries;
>
> (ii) these products are offered at prices which are substantially below those prevailing for similar goods of comparable quality in the market of the importing country. Such prices shall be compared both with the price of domestic product at comparable stage of commercial transaction, and with the prices which normally prevail for such products sold in the ordinary course of trade and under open market conditions by other exporting countries in the importing country."

This provision, together with the second condition that safeguard measures under the MFA can only be applied to products or countries whose exports of such products are causing market disruption, demonstrates an important difference between Article XIX and Article 3, i.e. Article 3 is selective in nature while Article XIX is non-discriminatory among all imports. The second difference is that under Article 3 substantial price undercutting can also be a cause, either as an independent cause or combined with the cause of increased imports, of market disruption. Thus, the scope for safeguard action under Article 3 is greater than that under Article XIX. In addition, in the determination of market disruption, it is required that account shall be taken of the interests of the exporting country, especially when the exporting country is a developing country.*103

As to the procedural requirements for taking safeguard action under Article 3, like in the case of safeguard action under the Draft Safeguard Code, it is essential that the invoking country shall consult with the exporting countries concerned.*104 If no agreement is reached in the course of consultation, the importing country is free to take safeguard action 60 days after the request for consultation was received by the exporting country concerned.*105 In highly unusual circumstances, the importing country may request the exporting country to cooperate in order to reach an interim arrangement, and is free to impose temporary restraints without regard to the 60-day limitation, when such interim arrangement is not reached.*106 Meanwhile, all developments including, inter alia , the request for consultation, the agreement reached in the consultation, and the application of safeguard measures as well as temporary restriction, extention of duration of a safeguard action, shall be communicated to the Textiles Surveillance Body.*107

An important feature of Article 3 is that it imposes several restraints on the application of safeguard measures. First, safeguard measures can only be applied to imports causing market disruption.*108 Second, when the market disruption was caused by imports from more than one country, the importing country in applying safeguard measures shall avoid discrimination among these exporting countries.*109 Third, the restriction shall not exceed the levels specified in Annex B of the MFA.*110 Fourth, the duration of a safeguard action shall not exceed one year, but renewal or extention for an additional year is possible when the exporting country so agrees. In the extended or renewed period, the safeguard measures shall be liberalized in such a way as stipulated in Annex B of the MFA.*111

Article 4 of the MFA allows participating countries to use bilateral arrangements in easing import penetration, without being bound by the conditions stipulated in Article 3.*112 The bilateral arrangements however are to be entered within a multilateral framework established by the MFA. This means the bilateral arrangements are subject to conditions set for their use and multilateral surveillance. Such bilateral arrangements shall be concluded on mutually acceptable terms and the terms shall be more liberal than those terms applied under Article 3. The permission to use bilateral arrangements in safeguarding domestic markets is in effect of little difference from legitimizing the use of VERs. This is because VERs in essence are a bilateral arrangement to regulate trade between two countries without regard to the state of the market conditions in the importing country. The only difference between the use of bilateral arrangement under Article 4 and the use of ordinary VERs, i.e. those not used in antidumping or other legitimate import restrictions, is that Article 4 sets the minimum terms for bilateral arrangements and makes them under multilateral surveillance as well as disciplines.

The safeguard scheme in the MFA is first loosened by the permission to use bilateral arrangements and further loosened by a conclusion adopted by the Textiles Committee in 1977, which allows departures from Article 3 and Article 4 when they are jointly agreed by the parties concerned and are reasonable.*113 However, the "jointly agreed reasonable departures" should be temporary. The jointly_agreed_reasonable_departure clause is much criticized as its frequent use would frustrate the whole structure of the MFA. Moreover, countries having small markets, an exceptionally high level of imports and a corresponding low level of domestic production, are allowed to disregard the restraints set in the MFA in order to maintain those countries' minimum viable production of textiles.*114 This rule is also known as the Scandinavian clause.

As to the organizational structure for the control of safeguard actions under the MFA, the Textiles Committee was established within the framework of the GATT to perform the same function as the Committee on Safeguard Measures. Under the Textiles Committee, there is a Textiles Surveillance Body whose major function is to supervise the implementation of the MFA. The TSB would review all reports sent to it regarding the use of safeguard measures by participating countries and thereafter report its findings to the Textiles Committee. When participating countries are unable to settle their disputes through consultation, the disputes can then be referred to the TSB which in turn will make recommendations.*115 Upon receipt of the recommendation, the participating country concerned should review the safeguard measure and contemplate their institution, continuation, modification or discontinuation.*116 Although the recommendations regarding the dispute are of no binding effects, they would be taken into account when the dispute is brought to the Contracting Parties of the GATT under the procedures of Article XXIII.*117 Before the dispute is referred to the Contracting Parties, it shall be brought to the Textiles Committee or the GATT Council for conciliation through the normal GATT procedures.*118

The linking-up of the dispute settlement procedures of the MFA and the GATT as an organization presents an important process of integration of the two. There are however some questions concerning the integration. First, the MFA is an agreement within the organizational framework of the GATT, and is not bound by the rules of the General Agreement. However, it is unclear whether the position of the MFA is in parallel with the individual rules of the General Agreement, e.g. Article XIX, or in parallel with the General Agreement itself. The Antidumping Code and the Subsidy/Countervailing Duty Code have their origins in the General Agreement, i.e. Article XVI and Article VI, and can be deemed as sub-agreements of the General Agreement. The MFA has no origin at all in the General Agreement. The origin of the MFA is the Long-Term Cotton Textile Arrangement of 1962 which was negotiated and concluded outside the framework of the

GATT. The MFA was first incorporated into the GATT system in 1973. It is stated in its preamble that the participating countries of the MFA are determined "to have full regard to the principles and objectives of the General Agreement on Tariffs and Trade" and in carrying out the aim of the MFA to implement effectively the principles and objectives agreed upon in the Tokyo Declaration.*119 The statement can be regarded as a demónstration of the MFA as a seperate and independent agreement from the General Agreement which would observe the principles and objectives of the GATT when they are not in conflict with the achievement of the aim of establishing orderly market conditions for textile trade. Moreover, the participating countries of the MFA are not necessarily the contracting parties of the General Agreement and _vice versa_ , whereas signatories of the Antidumping Code are necessarily the contracting parties of the GATT, although not _vice versa_ . Second, if the MFA is not a sub-agreement of the General Agreement like the Antidumping Code, there will be difficulties in organizational integration. As mentioned previously, the implementation of the MFA is carried out by the TSB and the Textiles Committee. However, these two organs have no power to authorize sanction against violation, and depend on the GATT Council and the Contracting Parties in this regad. The procedural rules for dispute settlement as provided in the MFA in effect place the Textiles Committee in the same position as the Antidumping Committee, and the TSB at a level lower than the Committee. However, if the MFA is to be considered as an agreement parallel to the General Agreement, the Textiles Committee should be equivalent to the Contracting Parties. Moreover, there are also difficulties in settling disputes arising from the MFA before the Contrating Parties. The dispute settlement as provided in Article XXIII is catered for disputes concerning nullification of benefits accruing to the contracting parties under, or the impediment of the attainment of the objective of, the General Agreement. A legitimate safeguard action under the MFA may well have the effect of nullifying the benefits accruing to the contrating parties under the General Agreement. An apparent example is that the MFA allows an importing country to take safeguard action on a selective basis, and the selective application of safeguard measure may in turn nullify the benefits of the MFN protection under the General Agreement. Third, there is also the problem of which agreement, the MFA or the General Agreement, has the preemption in application. It is provided in Article 9 of the MFA that the participating countries shall, "as far as possible", refrain from taking "additional" trade measures which may have the effect of nullifying the objectives of the Arrangement.*120 The language is ambiguous and the rule is limited to additional measures rather than substitute measures. Article 1:6 of the MFA provides that "the provisins of this Arrangement shall not affect the rights and obligtions of the participaing countries under the GATT". This provision gave justifiction for some developed countries, who felt the MFA was unable to meet their needs, to take safeguard actions under the General Agreement without first having recourse to Artice 3 or 4 of the MFA. The MFA imposes stricter constraints on the use of safeguard measure, though the conditions for the invocation of safeguard clauses are less stringent. Safeguard measures under the MFA are subject to various limits such as the base levels and growth rates. The issue of whether a participating country of the MFA which is also a contracting party has the obligation to exhaust the safeguard mechanism of the MFA before resorting to the

GATT procedure was discussed in a Textiles Committee's meeting in 1976, and participating countries could not reach a consensus on this issue. It is stated in the Conclusion of the Committee's 1981 Meeting that "in order to ensure proper function of the MFA, all participants should refrain from taking measures on textiles covered by the MFA, outside the provisions therein, before exhausting all the relief measures of the MFA".*121 Thus, as far as those participating countries of the MFA, who are also contractig parties of the General Agreement, are concerned, the MFA preempts the General Agreement.

CONCLUSION

The emergency safeguard clause provided in the General Agreement was originally designed for seasonal or other short-term changes in the circumstances of trade. However, because of the changes in the structure of the world economy, events that influence trade conditions have become permanent in nature. Secular changes require long-term adjustment policies rather than temporary safeguard measures. The use of safeguard measure in meeting with secular changes would lead to changes in the nature of safeguard measures, i.e. from temporary to permanent. The Draft Safeguard Code presents a sounder system which in many respects is similar to the MFA in general and Article 3 of the MFA in particular. The Code establishes a Committee on Safeguard Measures which is to conduct consultations and to keep national practices under surveillance. Meanwhile, several crucial questions are still unsettled. They include, among others, the causation standard, the right to retaliate, and most importantly the issue of selective application of safeguard measures. However, the whole structure of the MFA would be in danger of being frustrated, if the "jointly agreed reasonable departure" clause is frequently used. The integration of the MFA into the GATT system has the problem concerning the jurisdiction of the Contracting Parties under Article XXIII, and there is a need to enlarge the scope of Article XXIII so as to accomodate disputes arising from the MFA. As to the legality of VERs, current rules of the General Agreement are insufficient to render a clear case of illegitimacy and the use of VER by private parties is to be dealt with by domestic or international antitrust regimes.

Footnote (Part Two, Chapter V)

1. M.Meier, "Externality Law and Market Safeguards: Applications in the GATT Multilateral Trade Negotiations", Harvard Int'l L.J. Vol.18, No.3, Summer 1977 pp.491, 502
2. H.G. Johnson, "Technological Change and Comparative Advantage: An Advanced Country's Viewpoint", 9 J. of World Trade L., I (1975), pp.13
3. J. Bhagwati, "Market Disruption, Export Market Disruption, Compensation and GATT Reform", 4 World Dev. pp.989 (1976) pp.1007-8
4. The bribery and compensation in such a case is a means to buy the right to invoke market-safeguard trade restrictions.
5. B. Sodersten, 'International Economics', p. 189
6. Ibid
7. Ibid
8. B. Hindley, 'Voluntary Export Restraints and the GATT's Main Escape Clause', pp. 14
9. B. Hindley, "Voluntary Export Restraints and Article XIX of the GATT", in J. Black and B. Hindley (eds), 'Current Issues in Commercial Policy and Diplomacy'
10. B. Hindley, see note 9, p.13
11. Ibid
12. Ibid
13. Ibid
14. H.G. Johnson, see note 2
15. BISD Vol.IV, pp.325
16. Article XIX para. 1(b)
17. Ibid, para. 2
18. Ibid
19. Ibid, para. 3(a)
20. Ibid
21. Ibid
22. see Part Two, Chapter I Sec.II, (B)(4)
23. Report on the Withdrawal by the United States of A Tariff Concession under Article XIX of the General Agreement on Tariffs and Trade, Oct.1951, Sales No. GATT/1951-3, Nov.1951
24. see note 22, (4) (a) (i) and (iii)
25. Chapter I of the Draft Agreement on Safeguards
26. Regulation (EEC) No.1439/74 of the Council of 4 June 1974
27. GATT/CP.2/Rev. a, Sec. 30, pp. 7, Vol.II/39
28. Havana Reports, Sec. aa, pp.83
29. United States Senate Finance Committee, Report on H.R. 10710, "Trade Reform Act of 1974", S. Rep. No.93-1298, 93d Congress, 2d Session (Nov.1974) Under the U.S. escape clause law, the increase in imports shall be the substantial cause of serious injury.
30. see Part Two, Chapter I, Sec.II, (B) (6) (b)
31. Under a rational safeguard system, three years should be sufficient when one considers the nature of Article XIX action, i.e. to be used to meet emergency (sudden surge in imports) which is supposed to occur within a very short time frame.
32. Investigation No.TA-201-5, USITC Publication 756, Jan.1976
33. There will be more detailed dicussions of elements of distortion in the determination of appropriate time frame later in this section.
34. The across-the-board rate of tariff reduction only applies to items that were listed in the negotiation list. A negotiating country could protect producers of a specific product by excluding that product from the list. But once a product was listed, there was no way to protect

producers of that product by negotiating a special rate, except in the case of high tariff disparity.
35. The volume of imports may vary both above and below quota levels.
36. It is inappropriate to use the time period prior to the negotiation, as any change in import volume in that period is unconnected with the effect of a new negotiation, when the market conditions in the current time period are extraordinary. There is therefore a need to find other alternatives to deal with the situation where there exists no sufficient current period of time during which market conditions are not extraordinary.
37. Trade Agreements Extension Act of 1951, Pub. L. No. 82-686, 72 Stat. 673 76:(a); Trade Expansion Act of 1962, Pub. L. No. 87-794, 76 Stat.872 301 (b) (1); Trade Act of 1974, 19 U.S.C. 2251 (b) (2) (1976)
38. see note 23
39. Chapter 1, para.2 of the Draft Code
40. see note 23
41. Sec.201, 19 U.S.C. 2251 (b) (2) (1976)
42. Bolt, Nuts, and Screws of Iron or Steel, Report to the President by the International Trade Commission, Investigation No. TA-201-2, USITC Pub. 747, Nov. 1975, View of Chairman Will E. Leonard
43. U.S. Import Weekly Review
44. Chapter 1 para.2
45. Ibid, para.1
46. Committee on Ways and Means, House of Representative, 93rd Congress, 1st Session, Press release and other materials relating to the Administration proposal entitled "Trade Reform Act of 1973" (later became the Trade Act of 1974), HR 6767
47. see note 32
48. Note 1 on pp.65 of the BISD 26S, (Definition of "like product" in Subsidy/Countervailing Duty Code); and Article 2:2 of the Antidumping Code, BISD 26S/172
49. Ibid
50. BISD II/188, para.8
51. BISD 1S/53, para.12
52. BISD 25S/49, para.3.2-3.4, para.4
53. The issue in dispute in this case with regard to definition of the term "like product" was whether vegetable protein including corn gluten, skimmed milk powder as well as animal marine and synthetic proteins would be considered as like products.
54. Ibid
55. see note 52
56. Mushroom, ITC (1980), 2 ITRD 5209
57. Ibid
58. Certain Motor Vehicles and Certain Chassis & Bodies Therefor, ITC 1980, 2 ITRD 524
59. Ibid
60. Mushroom, see note 56
61. Chapter 1, para.4 of the Draft Code
62. Ibid
63. Certain Motor Vehicles and Certain Chassis & Bodies Therefor, see note 58
64. Chapter 1, para. 1 of the Draft Code
65. see Part Two, Chapter I(A), Section ii, (C)(1)(b)
66. Trade Agreements Extention Act of 1951, see note 38
67. Trade Expansion Act of 1962, see note 38
68. Eyeglass Frames, TEA-I-10, TC Pub.No.219 Oct.1967, 32 Fed. Reg.

14167 ; Piano, TC Pub. 3409
69. Trade Act of 1974, Section 201, 19 U.S.C. 2251 (b) (2) (1976)
70. Ibid
71. see note 32
72. see note 58
73. Investigation No.TA-201-31, US I.T.C. Pub. No. 894; 43 Fed. Reg. 27, 908 (1978)
74. see note 42
75. Chapter 1, para.2 of the Draft Code
76. Chapter 2, para.1
77. Ibid
78. Chapter 2, para.3
79. Chapter 2, para.4
80. Chapter 3
81. Chapter 3 (a) (b)
82. Chapter 3 (e), see also Article 3 of the MFA
83. Chapter 3 (c)
84. Chapter 5, para.2
85. Chapter 5, para.1
86. Chapter 5, para.7
87. note 17 of the Draft Code; Several GATT organs have the authority to conduct examination without initiatives from complaining parties, such as the Committee on Balance of Payments and the Textile Committee
88. Chapter 6, para.6
89. Chapter 6, para.8
90. Chapter 6, para.9
91. Chapter 6, para.10
92. Chapter 7, para.7
93. Chapter 7, para.3
94. Chapter 7, para.2
95. J. Tumlir, "A Revised Safeguard Clause for GATT?", 7 J.W.T.L. p.404
96. Article XI reads as follows.

> "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 destined for the territory of any other contracting party." BISD Vol.IV p.17

97. G.A. Res. 3563, U.N. Doc. A/RES/35/63; The Code was derived from the Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices approved by the UN Conference on Restrictive Business Practices on April 22, 1980. U.N. Doc.TD/RBP/CONF/10 (1980)
98. Arrangement Regarding International Trade in Textiles BISD 21S/3; Protocol Extending the Arrangement Regarding International Trde in Textiles, BISD 24S/5; Protocol of Extension (1982), GATT Newsletter, Focus , 10 January 1982
99. Article 3, para.2
100. i.e. employment, turnover, market share, profits, export performance, volume of disruptive and other imports, production, utilization of capacity, productivity and investment.
101. Appendix A of the MFA, I
102. Appendix of the MFA, II
103. Article 3, para.2
104. Article 3, para.3
105. Article 3, para.5

106. Article 3, para.6
107. Article 3, para.3
108. Article 3, para.2
109. Ibid
110. Under normal circumstances, the level below which imports my not be restrained shall be the level of actual imports or exports of the product in issue during the tweleve-month period terminating two months preceding the month in which the request for consultation is made. see Appendix B of the MFA,1
111. The level of each subsequent period shall not be lower than the level specified for the preceding tweleve-month period, increased by six per cent. The growth rate can be lower if the six-per cent rate would exacerbate the situation of market disruption. Appendix B of the MFA, 3
112. Article 4, para.2
113. Conclusion of the Textile Committee adopted on December 14, 1977, para. 5.3
114. Article 1, para.2
115. Article 11, para.5
116. Article 3, para.5 (iii)
117. Article 11, para.10
118. Article 11, para 9
119. The appearance of such language is a demonstration of the independent identity of the MFA. Otherwise, it would be unnecessary to reassert the GATT principles and objectives, if the MFA was a part of the General Agreement. In the case that an agreement is a sub-agreement of the General Agreement, like the Subsidy/Countervailing Duty Code, no such reassertion of the GATT principles and objectives appers in its preamble. Moreover, in a 1976 meeting of the Textiles Committee, one representative indicated that Article 3 of the MFA and Article XIX of the General Agreement existed in parallel. This is a further indication that the MFA and the General Agreement stand in the same position within the organizational framework of the GATT.
120. Article 9, para.1
121. Conclusion of the Textiles Committee adopted on 22 December 1981, GATT Newsletter, Focus , 10 January 1982

** The text of the Draft Code used in this thesis appears in Lowenfeld, 'Public Controls on International Trade', 1979 edition, pp. DS-560-DS-571

PART THREE

LAW, POLITICS AND EFFICIENCY

Chapter I

The Making and Application of Trade Laws

Part Three

As discussed in Introduction of this thesis, global efficiency and its resulting welfare effects are the primary aims of international trade and the post-war multilateral efforts towards trade liberalization. However, trading countries are equally, if not more, concerned about distribution of world income. Distribution problems in both international and domestic contexts are the sources of political pressure on national governments. While consumers may favor cheap imports, domestic producers may resent the idea of free trade if they are in danger of being outcompeted by imports. Although free trade can maximize world income, some countries who are losers in international competition may receive less of the increased wealth or even have a negative gain from trade.

Political pressures on trade liberalization can be eased through the application of the general principle of reciprocity, which would maintain to some extent the balance of interest between trading nations. However, only part of the pressures has thus been eased. There are residual pressures which tend to be inflated in time of economic hardship. We have discussed in Introduction how these residual pressures have affected the application of some of the general principles of trade law. How, then, do these residual pressures affect the making and application of specific trade laws? We have discussed the economics as well as legal structures of those trade laws where political pressures appear to be most imminent under current economic climate. The intention of Chapter I of this concluding part is to analyze the political elements in the making and application of those trade laws. It is noteworthy that the making of some of the trade laws is a response to political pressures, whereas some others are aimed at trade liberalization but have been weakened by protectionist forces. Moreover, there are also instances where because of insufficincy of legal techniques, law cannot fully reflect its underlying economic aim.

Chapter I will also go a step further to compare the possible distortive effects of those trade laws. Other than the existing distortion resulting from the existence of the laws themselves, this chapter will also demonstrate the maximum distortion that can be caused by protectionist application of trade laws under political pressures. This is because distortive effects may vary with the strength of political pressures and the only measurable one is the maximum effects. The intention of making such a comparison is to search for the relative position of each trade law in terms of distortive effects. The result will be used in Chapter II where attempts will be made to search for politically viable means for reform of these trade laws so as to minimize the inevitable trade distortion. Chapter II will introduce and comment on various proposals put forwards by lawyers and economists. Basing on the comments and the result of investigation of Chapter I, this thesis will then introduce its own proposals.

Chapter I: the Making and Application of Trade Laws

Section I: Domestic Antidumping and Countervailing duty laws

One way to distinguish domestic antitrust and unfair competition laws from antidumping and countervailing duty laws is that in the former case trade conflicts mainly exists between individuals within a national boundary, *1 while in the latter case trade conflicts exists in several relationships : (1) that between domestic and foreign producers, (2) that between domestic producers and domestic consumers, and (3) that between the governments of trading nations. The existence of rivalry between foreign and domestic groups may give a national government a easier way out in deciding which group should be given more weight. On the other hand, in the case of domestic antitrust law where conflicts of interest mainly exist between domestic groups, national interest would require the use of efficiency in allocation of domestic re- resources as the criterion. In the case of unfair trade practices law, the underlying rationale for such a legislation in somewhat different. The more relevant concept is the fairness in doing business which does not always coincide with the notion of efficiency. When a trader infringes his competitor's trademark, or practices false advertising or price discrimination among domestic markets, his action is in violation of the fairness in doing business. Hence, those whose interests are damaged by such action, be it other competitors or consumers, should be compensated. However, the notion of fairness may run in conflict with the notion of efficiency. For instance, recent develoment has shown that the ban on price discrimination in the domestic context may in many cases result in inefficiency.*2 Commentators have therefore called for modification in laws regarding unfair trade practices, especially price discrimination.

In the case of dumping and subsidization, domestic producers whose products are in direct competition with foreign imports unit as a group and exert pressure on their government to take counteraction, claiming that foreign producers are unfairly benefited from government subsidies or the monopolistic power in their home market. The process in reaching a decision of whether to take counteraction is purely a political play. The government is under pressures from several sources: domestic producers including those workers employed in the industry concerned, domestic consumers and foreign government. Difficulties to a specific sector caused by foreign factors rather than domestic policies often present a stronger argument for protection. Nationalism is always the preoccupation of a national government. This is especially so when the argument for protection is enhanced by the notion of faireness. Domestic consumers are not so organized as producers who in many instances are monopolists or oligopolists in the domestic market, and their voices are weak. They ususally depend on protection from the government which in this case may feel constrained in helping them. Foreign governments usually try to protect their trade interests through political channels before bringing a dispute to the international trade forum. However, their pressures are not so imminent as those of domestic producers. The protectionist trend has greatly enlarged the scope for the application of antidumping and countervailing duty laws. Thus, antidumping and countervailing duty laws are so administered that, far from the purpose of removing distortion, if there ever exists such a purpose in national legislations, they themselves become trade barriers. This is especially true in antidumping administration, because it does not directly involve the government of the exporting country, and relatively more politically neutral.

What are the effects of dumping/antidumping and subsidy/antisubsidy on global efficiency. As discussed in Chapter II of Part Two, dumping is not necessarily distortive. The only clear case where dumping is likely to result in distortion is when the dumper in a attemp to monopolize the importing market charges at prices below the maiginal cost of production. Nonetheless, in international context, such pursuit is difficult to succeed. The real distortive element of dumping lies in the condition of the dumper's home market. Such distortion of course can not be removed by the application of antidumping measures of an importing country. Whether a specific subsidy is distortive is also difficult to tell, as the definition of a distortive subsidy involves so many unsettled comlexities regarding the notion of external economies. Since the distortive effects of dumping and subsidy are at most uncertain, the use of countermeasures against these practices would very likely result in distortions. Apart from the actual imposition of countermeasures itself, the proceeding in reaching a decision as to whether to take counteraction sometimes is even more of a distortive element as its harassing effects on foreign producers and the resulting uncertainty in transactions would also affect allocation of resources.

Fairness and Comparative Advantage

The notion of fairness which provides an important argument for protection against foreign imports is not without difficulty. The argument goes like this: in the case of dumping, a dumper's ability to sell at low prices in foreign markets is made possible by the higher prices in his home market; and in the case of subsidy, government assistance provides foreign competitors with unfair advantage. The crucial points are therefore (1) whether a dumper's ability to maintain high prices at his home market is unfair, and (2) whether government subsidies are unfair advantages. What is the definition of "unfair"? The only possible way to define is through the notion of comparative advantage? What is then fair comparative advantage? The answer is not an easy one.

As mentioned in Part One, more advanced technology, more abundant supply of labour or energy, greater environmental assimilative capacity, and more harmonious industrial relations are commonly recognized sources of comparative advantage and therefore fair advantages. The second and less clear line of source of comparative advantage includes tax system, pollution control standards, antitrust policies, the protection of labour welfare and etc. At the bottom are those government selective policies purely for the improvement of exporters' competitivenes or the competitiveness of a specific import-competiting industry.

A dumper's ability to practice price discrimination is usually made possible by the monopolistic position in his home market, some kind of arrangement between producers to limit competition in the home market, and/or high import barriers imposed by the dumper's home country. These enabling factors can be put either in the second or the third line of source of comparative advantage depending on whether the conditions are created only for the purpose of meeting competition in a specific product trade. For instance, a monopolistic market structure may be the result of the government general policy to impose less stringent control on competition in pursuit of a social goal, or the specific policy to loosen control on the competition of a specific line of product. In the case of subsidy, government subsidies may be a part of the social system, or only for providing assistance to exporters or producers in the import-competiting industries.

As the enabling factors of dumping and the nature of a subsidy may fall either in second or in third line, it is rather difficult to conclude that all dumping or subsidy practices are unfair. The above distinction of first, second, and third lines only shows the degree of acceptance, and there exist no clear distinction as to the dividing point beyond which comparative advantage is considered as an unfair one. It also provides no guidance for the application of law. A trade legislation imposing restraints on imports, which is only based on the unsettled notion of fairness, could hardly be justified.

Section II: Article VI and the International Antidumping Code

The legislative intent of the GATT law on dumping is two-fold: to authorize importing countries whose domestic industries are injured by dumped imports to take counteraction, and to regulate antidumping administration in order to prevent it becoming a trade barrier. As to the former, both Article VI and the International Antidumping Code do not make it clear what the rationale behind the right to retaliate against dumped imports causing injury is. It could be a concession to protectionist pressure, the notion of fairness or the conception that dumping is generally distortive. In any case, the recognition of the right to retaliate is a departure from the norm of global efficiency. The distortive effects can be greatly reduced, if its administration is subject to effective discipline. However, one discouraging fact is that the International Antidumping Code follows the general pattern of pre-existing national antidumping laws, especially that of the U.S., and inherits some of their protectionist elements. The encroachment of politics can be seen not only in the making of substantive rules but also their application. There are at least four areas in the statement that "dumping... is to be condemned if it causes or threatens injury to an established industry...", where politics can exert its influence. They are: the definition of dumping, the indicia of injury, the quantum of injury required, and the necessary degree of causation between dumping and injury. The determination of dumping is to be made by comparing the price at which the import in question is sold with its normal value. Normal value is to be determined in a market where the product in question is sold in the normal or "ordinary" course of trade. When there is no sale in the ordinary course of trade, normal value may be constructed by adding a reasonable profit to the cost of production and other costs. The absence of a definition of the term "ordinary course of trade" enabled national authorities to regard sales at prices below the average total cost in the domestic market of the exporting country as not "ordinary", and apply constructed value in making price comparison. This is disastrous for exporters of those products with large fixed costs, because sales at prices below the average cost but above the marginal cost are common pactices in order to maintain production throughout recession. This could be exemplified by the EEC's approach in combating the penetration of petrochemical products from the U.S. The same can be said about the U.S. Trigger Price Mechanism. Under the TPM, sales at prices below the trigger price, calculated on the basis of the cost of production of the most efficient producer together with a reasonable profit, though not considered a dumping automatically, would trigger an antidumping investiation proceeding. The TPM is in fact an effective implementing instrument of the rule embodied in the U.S. antidumping law that sales at prices less than cost of production shall be excluded from being a criterion in the determiation of dumping. The basic price machanism used in the EEC Davignon Plan went a step further. Sales below the production-cost-based basic prices would be met with automatic and immediate levy of provisionl antidumping duties, unless exporters agree to raise prices and refrain from bringing complaint to the GATT. Such applicaion of antidumping law is in effect making it perform the same function as that of tariff law, and therefore a protectonist intrument.

If global efficiency and consumer welfare of the importing country are the prime concerns, the indicia of injury in an antidumping legislation should be stipulated in terms of the effects of dumping on competition in the domestic market, instead of business losses of domestic producers. Partly because of inheriting from national antidumping laws, partly because of the reluctance of the Code's signatories to make concessions, the Code does not require that in assessing injury reference be made to the condition of competition in the domestic market of the importing country. Nor does it provide any exception for dumping having positive effects on competition.

With regard to the quantum of injury, the higher the injury standard, the less distortive the antidumping administration. The Code only provides that injury shall be material injury and gives no definition for the term "material injury". A GATT working party in the

1960s in an attempt to substantiate the term equated it with substantial injury. Such an interpretation is not incorporated into the Code. With the empty concept of material injury, the Code provides an opportunity for signatories to broaden their application of antidumping law in response to domestic political pressure. The U.S. implementing legislation defines material injury as injury which is not "inconsequential, immaterial or unimportant" and is therefore able to continue its pre-1979 practice which does not differ much from the de minimis practice of the late 1960s.

Another area of confusion which also provides room for maneuver concerns the causal link required between dumped imports and the injury. A stringent causation test could greatly reduce the possibility of an affirmative injury determination. The 1967 Code requires that dumped imports be the principal cause of injury. The term "principal cause" was variously interpreted and was deleted from the 1979 Code. The vague language that "the dumped imports are...causing injury..." brings even more confusion and further widens the gap between different interpretations. In one extreme, this can be interpreted as the dumped imports need only be a cause of the injury. In the other extreme, the dumped imports should be the only cause of injury.

An overall evaulation of the substantive rules of the International Antidumping Code is that despite one of its legislative intents is to prevent antidumping administration from impeding trade flows, the Code turns out to be an endorsement of national practices and provides room for maneuver as domestic political situations so require. The protectionist practices of national antidumping authorities have transformed antidumping law into a new form of tariff law.

The above evaluation is however limited to the substantive rules of the Code. The procedural rules of the Code do tighten the control on national antidumping administration. The Code provides elaborate rules on every aspect of an antidumping proceeding, including simultaneous consideration of injury and dumping at certain stages of the proceeding, public access to information, protection of confidential information, imposition of time limits, imposition of conditions on the use of provisional measures, and prohibition of retroactive application of antidumping duties. Less political pressure can explain the relative easiness in disciplining the procedural aspect of national antidumping practices. This is because procedural rules do not directly affect the interest of domestic producers; rather, it is the exporters who are directly affected by procedural rules. In other words, improvement in procedural matters may provide greater safeguards to exporters without significantly reducing protection accorded to domestic producers. In addition, the use of basic price system can be challenged either by resort to the procedural rules of the Code or to the non-violation nullification or impairment clause.

Section III: Article XVI and the Subsidy Code

The GATT Subsidy Code (excluding that part of the Subsidy/Countervailing Duty Code which regulates the use of countervailing duties) is intended to establish a framework for the control of subsidy practices with the recognition that subsidies may have harmful effects on trade and production. If global efficiency is the only concern of such a law, subsidy practices should be prohibited except those ensuing no distortive effects and those used to correct existing market distortion. Under the Code, export subsidies are considered distortive per se and their use is prohibited unless the subsidizing country can rebut the presumption of adverse effect of the subsidy in issue. However, in order to reconcile with the political needs for granting subsidies to certain primary products and domestic subsidies, the use of these subsidies is given more tolerance. How far do these two arrangements depart from the goal of global efficiency?

As noted in Chapter I of Part Two, export subsidies are in most cases distortive unless they are accompanied by import levies at the same rates or used to correct distortion in the trade sectors. These two exceptions rarely exist. Under the Code, only those export subsidies that ensue adverse effects on the interest of another country and are objected by the country can be removed. This creates a gap between the goal of global efficiency and what can be achieved under the Code. The Code in an effort to bridge the gap provides that those adverse effects essential for a case of nullification or impairment are presumed to exist, when an export subsidy is found to exist. Secondly, even if a distortive and harmful export subsidy is objected by another country, it is possible that it will not be totally eliminated. There are two remedies available for a country whose interest is injured by a subsidy: countervailing duties and the dispute settlement scheme provided in the Code. A general rule is that distortion shall be corrected at their sources. Seeking remedies under the dispute settlement scheme which encourages disputants to reach a mutually acceptable solution does not mean the subsidy in question will be removed. It is more often than not that the practicing country will offer some other concessions to compensate the complaining country. The most notable instance of this kind is the trade-off between the U.S. DISC export subsidy programme and the tax exemption granted by some European countries for incomes earned outside the territory of the taxing country. Countervailing duties by their nature as a self-defense machinery are directed at the elimination of the effects of a subsidy on the industry of an importing country, rather than the elimination of the subsidy itself. Thirdly, when a complaining country prefer to seek remedy through the dispute settlement scheme and insists that the subsidy be removed, there are still cases where distortion can not be corrected. This can be exemplified by the exemption method adopted by some European countries in dealing with international double taxation. Though the exemption method may benefit exporters by exempting activities carried out outside the territory of the taxing country and was considered as a subsidy practice by an investigating panel, its historical backgrounds and the technical difficulties involved make its removal impossible. The difficulty in defining subsidies also creates similar problems. In many instancs, the definition of subidy is confronted with the choice between commercial rates and cost of government assistance. In the case of export credit and export quarantee, the Code stipulates that official export credit or guarantee at rates unable to cover the cost of financing is a subsidy practice. Such definitions are required by the general rule laid down by the GATT working parties that a subsidy shall involve government funds or budgetary deficits. However, as economists point out, providing credit or guarantees at rates lower than market rates would affect allocation of resources and result in some degree of distortion. The efficiency issue is furthr complicated by the prevalence of subsidies in export financing and the existence of internaionl arrangemnts setting minimum rates totally unconnected with commercial or cost considertions.

With regard to export subsidies on certain primary products, and subsidies other than export subsidies, national governments participating in the negotiation of the Code were deterred by their domestic political pressures from entering a full commitment to eliminate these subsidies. Export subsidies on certain primary products are not prohibited unless they result in the practicing country having a more than equitable share of world export trade or material price undercutting. Violation of such a rule will not be necessarily held responsible or required to remove the subsidies so long as they do not cause adverse effects on the interest of a complaining country. Subsidies other than export subsidies are not presumed illegal and a practicing country will be held liable only when the subsidies cause adverse effects on the interest of other countries. Basically these two sets of rules regarding the use of export subsidies on certain primary products and subsidies other than export subsidies are not different from that on export subsidies, because in all three cases a country will not be held responsible unless its subsidy practice results in necessary adverse effects. The main difference lies in the burden of proof in establishing a case of nullification or impairment. Export subsidies are presumed to result in adverse effects necessary for the establishment of a case of nullification or impairment and since the use of an export subsidy is a violation of the rule, it would not be difficult to demonstrate the reasonablly expected benefits. Moreover, in requesting for consultation which is the starting point of the Code's dispute settlement proceeding, a complaining country is only required to produce evidence regarding the existence of a subsidy, and the defending country has to prove that there is no subsidy or there is no adequate adverse effects. The same rule applies to export subsidies to certain primary products except that the presumption of the existence of adverse effect is valid only when the subsidy in issue has resulted in the defending country having more than an equitable share of world export trade or resulted in material price undercutting. Such presumption does not apply to subsidies other than export subsidies, and a complaining country in requesting for consultation will have to produce evidence of the existence of a subsidy as well as nullification or impairment of benefits. The difference in the burden of proof is significant because of the difficulty in establishing a case of non-violation nullification of benefits, which in the present case means a case of nullification of bnefits based on the use of export subsidies other than export subsidies. To establis a case of nullification of benefits without the convenient presumption, a complaining country has to demonstrate what benefits have been nullified, and prove whether the practice nullifying its benefits is not within its reasonable expectation and the adverse effect is serious enough. Several attempts to establish a non-violation nullification case under Article XXIII which is the origin of the Code's dispute settlement scheme failed, simply because the complaining countries were unable to demonstrate what benefits other than tariff concessions have been nullified. As to the issue of reasonable expectation, previous cases teach that the GATT investigating panels were cautious in determining whether a practice which nullified another country's benefits was within the expectation of the country, and decisions heavily depended on specific conducts of the defending country, especially those conducts in negotiating concessions. Such specific conducts are easier to identify in the negotiation of product-by-product concessions but more difficult to identify in the negotiation of across-the-board tariff reduction and even more difficult in the negotiations of non-tariff concessions, such as the negotiation of codes of conducts. Although the necessity of maintaning the requiremet of reasonble expecation is very much in doubt, there is no clear indication either in the statutory or case law of the GATT that the requirement shall be removed. As to the quantum of adverse effect, no clear guidelines have ever been laid down.

When a complaint is brough to the Committee on Subsidies and Countermeasures under the serious prejudice clause or material injury clause, rather than the nullification clause, export subsidies, export subsidies on certain primary products and subsidies other than export subsidies are treated equally. In other words, in all three cases, the complaining country has to prove the existence of injury or serious prejudice. However, the difference in procedural requirements for consultation remains.

The main weakness of the Subsidy Code is that it does not encompass such a notion of non-distortive subsidies, i.e. some general subsidies, subsidies used to correct existing distortion, and export subsidies accompanied by import levies at the same rates. It may be that the Code when assuming all injurious subsidies are distortive only makes distinction between injurious and non-injurious subsidies. Authorizing countermeasures or allowing imposition of countervailing duties against such subsidies would in fact increase the level of protection to the domestic producers of the country taking counteractions. Incorporation of such a notion can be through a change of the legal definition of subsidy from gross to net subsidies, i.e. from subsidies received by the producers of the product concerned to subsidies effectively change the competitive position of the producers receiving them to other producers. Moreover, there is also a need for an exception for subsidies intended to correct distortions but the divergence in economic philosophies may make the definition of such subsidies difficult. If these two innovations can not be achieved, there are other ways to remedy the deficiency. An exporting country can make complaint to the Committee, claiming that the imposition of countervailing duties nullifies the benefits under the Code that non-distortive subsidies would not be met with countermeasures because the Subsidy Code is only intended to eliminate distortive subsidies. However, if the case is brough to the Committee by an importing country or a third country claiming that its trade interest has been adversely affected by a subsidy practice, the Committee will rule according to the Code and probably makes a non-distortive subsidy but an injurious one subject to countermeasures. Under such circumstances, the exporting country can bring the case to the Contracting Parties under Article XXIII. The difficulty in such a pursuit is that the jurisdictions of the Committee and the Contracting parties have never been clearly defined and whether the Contracting Parties has the right to overrule the Committee's decision is yet to be clarified.

In general, the Subsidy Code is not seriously crippled by political pressures. All subsidies are subject to the same legal constraints and the only difference is the burden of proof in establishing a case of nullification which is one of the three causes of action that a complaining country can employ in seeking remedies. There are precedents where a complaining country was unable to establish a case of non-violation nullification, yet still able to make a successful claim under the serious prejudice clause. The Code is rather handicapped by the GATT's legal structure under which non-injurious conducts or conducts not objected by other parties would not be removed, although they result in distortions. The deficiency in coping with non-distortive subsidies can be remedied by making a counterargument based on the Code's legislative intent. However, there is also the difficulty in deciding which subsidy practice is distortive and there is a need to establish a framework within which multilaterally negotiated criteria can be produced.

Section IV: Article VI and Countervailing Duty Code

The pattern of the Countervailing Duty Code is essentially the same as that of the International Antidumping Code and therefore bears some of the protectionist characters of the latter. However, these protectionist elements in countervailing duty law do not contradict the aim of global efficiency, as countervailing duties can offset the distortive effects of a subsidy on the domestic industry of an importing country, although probably a large portion of the distortive effects existing outside that country remains. There are however two exceptions. The imposition of countervailing duties is not preconditioned that the subsidy in issue should be distortive. Therefore, it is possible that countervailing duties would create distortion when the subsidy in issue is not distortive. Another case of distortion that may be resulted from the application of countervailing duties is that national authorities always have the temptation to impose the duties to the maximum of the margin of subsidy, regardless of the actual effect of the subsidy on the price structure of the product in question. Moreover, countervailing duties is an insufficient instrument, if not inappropriate, in eliminating distortions created by a subsidy, because it only aims at the effect of the subsidy on the importing country.

As to the distortive effects of countervailing duty administration, the Code tightens the procedural requirements for such administration and greatly eliminates its harassing effects. One of the side-effects of the tightening of the procedural requirements such as the imposition of time limits, is that it reduces the discretionary power of national administrating authorties. This in turn greatly eliminates the flexibility of countervailing duty administration, which is an important element in minimizing the damaging effects of the use of countervailing duties on international trade relations.

The Countervailing Duty Code does not follow the Subsidy Code as to differentiate treatments accorded to different kinds of subsidy. An importing country can impose countervailing duties against all kinds of subsidies, so long as the administrating authority determines that its domestic industry is injured by subsidized imports. The complaining domestic industry and the administrating authority are responsible for producing evidence regarding the existence of a subsidy and injury. This is to ensure that the self-defense machinery would not be misused.

One must however distinguish abuse from misuse of countervailing duties. Imposition of countervailing duties may have enormous international repercussions as the practice may be resented by governments of exporting countries who feel imperative to assist their industries. This is especially true when one takes into account the low injury standard and the highly critical attitude towards the definition of subsidy of some national countervailing duty law, especially that of the U.S., together with domestic pressures to act against imports, would make a government action easily fallen into the definition of subsidy and every subsidized imports countervailable _per se_. Moreover, the divergence in economic philosophies among trading nations may seperate them further, if countervailing duties are carelessly used. The problem may become more serious when a subsidy is considered by the practicing country as efficiency-enhancing for it is designed to correct existing market distortion. For such politically sensitive cases, the proper channel to seek remedy is the Code's consultation-conciliation facilities. The GATT investigating panel is better able to stand neutral in adjudicating whether there exists a subsidy and whether the injury caused is serious enough. Meanwhile, through consultations, disputants can reconcile with each other and even lay down precedents for future cases. This approach can also provide the government of an importing country an exit from the difficult situation where both domestic producers and foreign governments exert pressure on it. To make such an alternative viable, there shall be certain degree of flexibility in antidumping administration and the administrating authority shall have enough discretionary power to suspend a domestic proceeding pending the litigation under the GATT dispute settlement scheme, and terminate the domestic proceeding when the investigating panel rules that the practice in issue is not a subsidy in violation of the GATT law or a mutually satisfactory settlement has been reached. Such discretionary power in the case of the U.S. was deprived from the administrating authority as the mounting protectionist pressure forced the legislative body to close any possible door through which a subsidized import can escape from the application of countervailing duties.

The complicated nature of subsidy practices and the inherent nature of countervailing duties as a self-defense machinery may raise the doubt of whether countervailing duties is still a proper measure to deal with subsidies, especially after the establishment of a multilateral mechanism for the resolution of an issue of multilateral concern.

Section V: Article XIX and the Draft Safeguard Code

Article XIX provides a safeguard mechanism for countries whose domestic markets are disrupted by a sudden increase in imports. The safeguard is intended to give import-competiting industries time to adjust to import competition by improving their efficiency and become competitive again, or to allow the industries to decline gradually with minimum social consequences. This is a necessary exception to the general rules of the GATT in order to reduce social as well as political costs of trade liberalization. However, abuse of safeguard action may frustrate other provisions of the General Agreement aiming at trade liberalization. Indeed, from an economic point of view, the need to have a safeguard clause is very limited, and it is often suggested that the use of safeguard measures be under strict international control.

Unlike the GATT antidumping and countervailing duty laws which are directed at the elimination of barriers to international trade while providing some exceptions to accomodate political considerations, the safeguard provision itself is an exception which creates trade barriers. Thus, the legal design of the safeguard system is necessarily different from that of antidumping and countervailing duty laws. First, the conditions for the use of safeguard measures are more stringent than those for the use of antidumping and countervailing duties. An importing country is allowed to take emergency action imposing quotas or raising tariffs only when there is an increase in imports which causes serious injury to domestic industry. Although the term "serious injury" has never been clearly defined, the common understanding is that the quantum of serious injury should be higher than that of material injury. Secondly, safeguard measures shall be applied to imports from all sources, whereas antidumping and countervailing duties can only be imposed on dumped or subsidized imports causing injury. The principle of non-discrimination is particularly important in preventing more efficient newcomers from being held soly responsible for market disruption. Thirdly, being a no-fault relief, a safeguard measure is subject to legitimate retaliation by exporting countries. The right to retaliate or to be compensated is an application of the legal (as opposed to economic) principle of reciprocity which is not only irrelevant to the aim of global efficiency but at times may restrict trade further. However, the right to retaliate is important in that it when combining with the principle of non-discrimination can effectively deter importing countries from taking safeguard actions without restraint and therefore may have positive effects on global efficiency.

A trading system without political considerations would rarely need a safeguard system. A less distortive safeguard system would impose strict conditions on the use of safeguard measures, require non-discriminatory application and place no restraints on the right to retaliate. Present safeguard system stands somewhere in between. The effort to reform Article XIX in the Tokyo Round failed to produce a safeguard Code, because of the controversy over the issue of selectivity. Except the selectivity issue, the Draft Code does provide a sounder safeguard system. Improvements include prohibition on the repetition of investigation on the same product for a period of time, progressive liberalization of safeguard measures, limitations on the duration of the measures and restriction on their extension, multilateral surveillance, special considerations for developing countries and procedural safeguards to all interested parties. No definition of serious injury has been reached, but there is a list of indicia of injury without specifying the necessary quantum. One important feature is that the Draft Safeguard Code although confirming the right to retaliate imposes certain degree of restraints on the exercise of such a right. Finally, it is possible that the final draft of the safeguard code would follow the revised antidumping and countervailing duty codes and adopt a simple causation test. As mentioned previously, there is a serious divergence in the interpretation of simple causation test. If the U.S. adopts the same interpretation in safeguard administration as that in antidumping and countervailing duty administration, the effort to tighten the conditions for the invocation of Article XIX will be frustrated. Thus, if the safeguard code adopts the simple causation test, it will be necessary to clarify its definition.

Section VI: Voluntary Export Restraints

A voluntary restraint on exports is an action of restraint by an exporting country taken voluntarily. The different attitudes towards the modifier "voluntary" reflect the controversial character of VERs.

One may say that the word is misused as exporters are usually forced to enter such an arrangement. On the other hand, when the alternative to an arrangement of VER is emergency action under Article XIX, antidumping or countervailing duties, import restriction under special legislations enabling the administration of an importing country to disregard international obligations, the word "voluntary" reflects its true meaning. VERs are as a distortive element as other import restrictions imposed under various legal regimes, but they provide a good way to compromise the interests of both exporting and importing countries. An importing country may find the existing legal constraints make it difficult to assert protectionism through legal mechanisms or the use of legal means may be antagonized by exporting countries as the legal mechanisms themselves may have been distorted by protectionism to some extent. VERs are also beneficial to exporting countries in that the shift in world income is in their favor. More on the positive aspect of VERs as an instrument to solve trade conflicts will be discussed in the Hindley proposition in the next chapter. A third country may however be vitimized by an arrangement of VER, because the market of the importing country will thereby be restricted and the third country will be obliged to absorb extra imports.

The legal status of VERs is also a controversial one. The issue has been challenged in domestic courts but never been brough to the GATT in the form of legal action for clarification. The central issue in this regard is whether an arrangement of voluntary export restraint can be regarded as a government action; as the GATT is only binding on government behaviours and does not intervene in private dealings. If an arrangement of VER can be regarded as an official agreement, it will be faced with two challenges: first, imposition of tariffs or quotas, either import or export quotas, except in certain cases is prohibited under the GATT and the legal effects of a VER arrangement is similar to the imposition of quotas by the exporting or the importing party of the arrangement; second, a third country may complain that its benefits under the GATT are nullified or impaired by the penetration of the extra imports excluded from the market protected by the arrangement. The first challenge is not a serious one, because the exporting country entering into such an arrangement will never challenge the legitimacy of the arrangement, thinking it the best arrangement attainable. As to the second one, a third country can seek remedy under Article XXIII, and what it can best achieve is the dismantling of the agreement and at least withdrawal of concessions to trade with the exporting and/or the importing parties to the arrangement. The most likely outcome is that the exporting country also undertakes a voluntary restraint on exports to the third country in question, because Article XXIII encourages disputants to reach a mutually acceptable solution and VERs appear to be the best chioce. Moreover, litigation under Article XXIII is a slow process and the third country may prefer to negotiate directly with the exporting country for a VER agreement without invoking Article XXIII. After the legal complications, the whole issue returns to the starting point,i.e. the dispute arising from the use of VERs is settled by another VER arrangement. Thus, it may make no legal sense to search for the illegitimacy of a VER arrangemnt in international context, as it is often short of a plaintiff or a plaintiff insisting on a remedy other than a VER arrangement.

An interesting connection between VERs and the GATT legal system is that in certain cases VERs are incorporated into the GATT system as a legitimate remedy. Apart from the notion of "mutually acceptable solution" in the dispute settlement proceeding of Article XXIII, which includes VERs, VERs also appear in the Antidumping and the Countervailing Duty Codes. An antidumping or countervailing duty administrating authority shall accept voluntary undertakings to revise the prices of the imports under investigation or take measures to eliminate the effects of the subsidized or dumped imports, when the offer is not impractical. There are several limitations imposed on the use of such voluntary undertakings, but a closer examination of such limitations reveals that they are not so powerful as to make voluntary undertakings of this kind, though legitimate, less distortive than ordinary use of VERs. Before explaining this proposition further, it is necessary to say that such voluntary undertakings are by no means more distortive than actual imposition of antidumping and countervailing duties. This latter proposition can also be explained in the following comparison between ordinary use of VERs and legitimate use of voluntary undertakings under the Antidumping and the Countervailing Duty Codes. An offer of voluntary undertaking can only be sought or accepted when an administrating authority has initiated an investigating proceeding, even without having reached a determination of subsidy or dumping. This requirement is not a significant one as a proceeding can easily be initiated, provided the complaining industry submits certain evidence the sufficiency of which is usually not under strict examination. Secondly, a voluntary undertaking shall automatically lapse if there is a negative determination of injury. It is more often than not that the final determination of injury will be positive, because of the extremely low injury test made possible by the ambiguous language in the codes. Thirdly, a voluntary undertaking shall not remain in force any longer than necessary to counteract the subsidization or dumping causing injury. However, the necessary length of time is to be determined by the investigating authority, while in the case of VERs the exporting country concerned can negotiate with the importing country on this issue. Fourthly, when a voluntary undertaking is to revise the prices of the imports, price increases shall not be higher than necessary to eliminate the amount of subsidy or margin of dumping. The upper limit is not necessarily lower than what an exporting country can achieve through the negotiation of a VER agreement, when one takes into account that in the assessment of the margin of subsidy the Countervailing Duty Code does not prohibit the use of gross subsidies and the amount of duty could be as high as the margin of subsidy, and in the assessment of antidumping duties the criterion used usually is the cost of production plus over-estimated profits.

Recent attempts to reform Article XIX also extend the coverage to the issue of VER. One of the proposals suggests that the conditions for the invocation of Article XIX be adjusted so as to attract either exporting or importing countries in a trade dispute to seek settlement within the legal framework of Article XIX rather than through the use of VERs.*4 The appropriateness of this proposal will be dealt with in the discussion of the Hindley proposition in the next chapter. Another proposal is to make the use of VERs under the discipline of Article XIX. The detail of this proposal is at present stage unclear as the GATT official documents reveal very little. One of the possibilities is to incorporate VERs into the framework of Article XIX, i.e. to allow VERs as a safeguard measure other than tariffs or quotas and make the use of VERs in this context subject to the discipline of Article XIX. This is in effect the same as the voluntary undertakings in the Antidumping Code and the Countervailing Duty Code. This is also not something new to the existing legal systems for this is the international application of the notion of "orderly marketing arrangement" embodied in the U.S. trade legislations. If acceptance of voluntary undertakings in a safeguard proceeding is made compulsory when it is not considered impractical, the major disadvantage of Article XIX to exporting countries that the shift in the distribution of world income is in the importing country's favor can be greatly reversed. However, VERs in this context shall be applied in such a way as to aviod being violative of the principle of non-discrimination.

Section VII: <u>Sectoral Exception to the General Rules of the GATT: the MFA</u>

The conclusion of the MFA is a recognition of political relaity in textile trade. The legal structure of the MFA is built on the following important provisions. Article 1 provides that actions taken under the MFA should be accompanied by appropriate social and economic policies to encourage adjustment and shall not interrupt or discourage autonomous industrial adjustment processes. Article 2 provides that with a few exceptions quantitative restrictions or other measures which restrict trade flows shall be terminated within one year of the entry of the MFA. Article 3 provides an exception to the general rule that no new restrictions on textile shall be introduced. Resort to the exception is subject to the following conditions: (1) there shall be market disruption caused by imports, (2) restriction can only be applied to the precise products and to the countries whose exports are causing market disruption, (3) restrictive measures shall be applied non-discriminatorily to exports of all countries causing market disruption, and (4) the levels of the base quota and its growth rate shall not be lower than the levels provided in the Arrangement. Article 4 provides a further exception and allows bilateral agreement, if (1) the agreements are concluded "on mutually acceptable terms" and (2) on overall terms, the base level and its growth rate shall be more liberal than those under Article 3. In addition, the Textiles Committee in 1977 adopted a crucial conclusion that the concept of mutually acceptable solution in Article 3 and 4 includes "the possibility of jointly agreed reasonable departure from particular elements in particular cases".

With a few variations, one can find that the MFA is in effect a combination of Article XIX of the General Agreement and another kind of legitimate use of VERs. In the following the distortive effect of the MFA in relation to those of Article XIX and ordinary use of VERs is examined.

(A) <u>Article XIX and Article 3</u>

Several points can be made from the comparison between Article XIX of the General Agreement and Article 3 of the MFA. First, safeguard actions under Article XIX is subject to the condition that domestic industry of the country taking action has been or under the threat of being seriously injured, while under Article 3 there shall be market disruption in that country. Determination of market disruption shall be based on "the existence of <u>serious</u> damage to domestic producers or actual threat thereof" (emphasis added) *5. Thus, although the terms used in both articles are different, the quanta of injury for invocation are the same. Second, serious injury under Article XIX shall be caused by increased imports, while under Article 3 by either sharp or substantial increase in imports or substantial price undercutting. Third, Article XIX safeguard measures shall be applied to all imports non-discriminatorily, while Article 3 measures can only be applied to those causing market disruption. Fourth, there shall be compensation under Article XIX, while with few exceptions no requirement as such under Article 3. Fifth, both articles impose limitations on the levels as well as duration of safeguard measures and provide progressive liberalization of these measures. Limitations under Article 3 are more specific and precise. Sixth, adjustment policies are encouraged under Article 3, and there are proposals in the negotiation of the Draft Code that there shall be a provision incorporated into the Code to the same effect.

From the above comparison, one can perceive that there will not be much difference between Article 3 and Article XIX, if the final version of the safeguard code imposes conditions on compensation, and allows selective application of safeguard measures. More importantly, the introduction of limitations on the duration and the levels of safeguard measures into Article XIX, together with the inclusion of the "reasonable departure" clause in the MFA, greatly narrows down the gap between Article XIX and Article 3 created by the growth rates and base levels provided in the MFA. The gap used to be the main reason for some importing countries to impose restrictions under Article XIX rather than Article 3. With the pattern of Article XIX approaching that of Article 3 and the more precise limitations on the use of safeguard measures under Article 3, it is hard to conclude that

Article 3 is more of a distortive element than Article XIX in international trade.

(B) Article 4 of the MFA and VERs

In practice, Article 4 has been more frequently used than Article 3, just like the relation between Article XIX and VERs. Under Article 4, VERs are allowed as a legitimate means of import relief, provided two conditions are fulfilled: arrangements shall be concluded on mutually acceptable terms and the terms shall be more liberal than those under Article 3. The first condition is without question as VERs imply the element of "mutually acceptable". The second condition is somewhat eroded by the interpretation made in 1977 that mutually acceptable terms include the possibility of jointly agreed departure. Nevertheless, as a general rule, any distortive measure whose use is subject to certain discipline is less distortive than without. Thus, the use of VER under Article 4 is less distortive than ordinary use of VERs.

CNCLUSION

We have examined two kinds of legislation: one having the effect of eliminting distortive elements including subsidy and countervailing duty laws, and the other having the effect of creating distortions including safeguard law under the GATT, the MFA, and antidumping law. There are also distortive VERs. Countervailing duties in some cases are distortive and they are an inappropriate instrument to correct distortions created by subsidy practices. Among those existing legislations, antidumping law appears to be the most distortive, because it allows national authorities to turn antidumping duties into a protective instrument. VERs are not more distortive than antidumping duties and they have several advantages as an instrument in solving trade disputes. VERs under the MFA are less distortive than ordinary VERs as the MFA imposes several limitations on the use of such VERs. VERs under the MFA is more distortive than Article XIX under the MFA,i.e. Article 3 of the MFA, because control on their use is less stringent than that on the use of safeguard actions. Article 3 may be more distortive than current Article XIX, because it can be applied selectively and without compensation, though with more stringent rules on the use of safeguard measures. If the safeguard code allows selectivity, imposes conditions on compensation and makes the conditions for the use of sfeguard measures more stingent, there will not be much difference between the distortive effects of Article 3 and Article XIX. With the distortive effect of each variable in mind, efforts are made in the next chapter to seek a proper formula which is politically viable and the least distortive, and can adequately compensate exporting countries subject to unjustified import restrictions.

PART THREE

LAW, POLITICS AND EFFICIENCY

Chapter II

In Search for A Solution

Chapter II: In Search for A Solution

Section I: Barcelo Proposal I *1

This proposal is dominated by the notion of efficiency, and urges national implementing legislations to place more emphasis on the efficiency consideration. It mainly deals with antidumping and countervailing duty laws, basing on the assumption that the safeguard clause in national trade laws can adequately cope with import-caused injury. With regard to antidumping law, Barcelo argues that dumping except predatory dumping is not objectionable and is consistent with global efficiency as well as beneficial to the consumer welfare of the importing country whose domestic market is penetrated by dumped imports. Thus, antidumping law itself is a barrier to trade and should be abolished. If this cannot be achieved, the second-best solution will be to apply antitrust injury test,i.e. injury to domestic competition rather than domestic producers, and a four-part test looking into predatory intention, market structure, competitive conduct, and cost information can be used to identify predation. There is no valid reason for granting protection against non-predatory dumping.

On the other hand, in the case of export subsidy, countervailing duties should be made mandatory, i.e. should be used without being preconditioned by the existence of injury to domestic industry. The reason is that the use of countervailing duty to offset the effects of an export subsidy which is distortive *per se* has a positive effect on the attainment of global efficiency. Exceptions are allowed for common export subsidy practices like subsidized export credit, and for agricultural products, regarding which there exist special international arrangements. Under such circumstances, countervailing duties can be used only when there are violations of these arrangements. Export subsidies accompanied by import tariffs at the same rate should be free from countervailing duties. With regard to domestic subsidies, i.e. subsidies other than export subsidies, different treatments shall be accorded to different types of subsidies. Firstly, when a country can prove its domestic subsidy practice is not distortive, the subsidy should be immune from countervailing duties. Secondly, there shall be special agreements to deal with domestic subsidies commonly used by trading nations, such as subsidies related to national defense, regional aids, subsidies to specific industries particularly in distress. Countervailing duties can only be used to sanction violations of these agreements. Thirdly, subsidies not within the previous categories will be subject to countervailing duties when they cause injury. The injury should be serious in degree and the subsidized import in question should be "a cause which is important but not necessarily more important than any other cause" of the injury. This causation test is similar to that applied in the U.S. adjustment assistance relief.

Comment

1. Barcelo's proposal on antidumping law is sound in the light of global efficiency. However, one has to take into account political reality in time of recession. Abolition of antidumping law is just like depriving a sick person or a person in extreme danger of a safeguard which he believes is vital to his survival, no matter whether the sickness or the danger is caused by the event to which the safeguard is supposed to apply or whether they can be cured by the safeguard. Only a healthy person is psychologically strong enough to be reasoned that its private interest has to be sacrificed for public

interest, and its legitimate interest can well be protected by other measures. Amendament of an existing legislation intended to tighten a remedy available for industries is much more difficult in time of economic hardship than in time of economic prosperity, even though the remedy is an inappropriate one. What one can best expect is to prevent the loosening of the conditions for the use of such a remedy. This can partly be done through multilateral consultation and dispute settlement facilities formally incorporated into the International Antidumping Code after the Tokyo Round. However, there is still a need to seek a less distortive means to ease domestic pressure for protection and release antidumping law from such pressure. The adequacy of Article XIX in performing such a function is doubtful. Article XIX is much more difficult to invoke to both domestic producers and national governments. It will not be acceptable to domestic producers, if they are to trade off the remedy under antidumping law for Article XIX remedy. International repercussions of Article XIX actions may make national governments prefer taking action under antidumping law which is relatively more politically neutral. Adjustment assistance is a remedy more costly to the governments of importing countries in terms of fiscal budget but more permissble under GATT law. Nevertheless, adjustment assistance though more permissible under international law may be difficult to obtain. In the case of the United States, the conditions for granting adjustment assistance are similar to those for escape clause remedy. To establish a case for adjustmnt assistance, there shall be serious injury, but the causation requirement is somewhat lower than that for escape clause action. An arrangemnt of VER may be an alternative. Another possibility is to negotiate international arrangments for such industries as steel, and car where recessionary impacts appear most serious. This alternative will be explored further in later sections.

2. With regard to export subsidies, it is not without difficulty in making countervailing duties mandatory. A subsidized import can benefits an importing country with cheap supply of goods. This is especially so when the import in question is an intermediate product. Under such circumstances, the export competitiveness of the importing country can be enhanced. It is therefore difficult to expect an importing country to apply mandatory countervailing duties in the absence of injury to domestic industry. The U.S. once maintained a mandatory countervailing duty regime, but the administrating authority usually hesitated to impose duties on non-injurious imports. Rather, the authority incorporated the notion of injury into its determination of subsidy. Any government assistance which did not result in significant trade effects was not considered as within the legal meaning of subsidy.

3. Barcelo's approach towards non-distortive subsidies is also not without difficulty. He does not clarify which institution, the administrating authorities of importing countries or the Committee, is to consider whether an exporting country's argument that its subsidy practice is not distortive. There is substantial ambiguity in the so-called "external economies", which provide important theoretical foundations for government interventions, as to what the social cost or social benefit is. Individual governments may have different perceptions of these issues and any attempt to control government interventions in this regard would require a certain degree of consensus among trading nations. Moreover, the timing and the form of assistance are often politically determined. It would be absurd to

let the governments of importing contries to make the decision as to whether a subsidy practice is distortive or not. One may also argue that countervailing duties can still be used when there are internationally agreed criteria based on the maximum consensus that can be reached. However, a rule-of-reason case (as opposed to a <u>per se</u> case) can never be adequately judged according to existing guidelines only, and there is no guarantee that domestic administrating authorities under domestic political pressure would evaluate the case in good faith. The proper forum for such a decision should be the Committee under which an investigation panel can be established to adjudicate the case according to the criteria reached in the course of previous consultations among the signatories and the special expertise of the panel's members. There are however two difficulties. Firstly, as mentioned previously, the Code does not encompass the notion of non-distortive subsidies. It only concerns injurious and non-injurious subsidies. Secondly, even if the Code incorporates such a notion and provides one way or another for non-distortive subsidies to escape from countervailing duties, there is still the problem of how to move the decision process from national administrating authorities to the Committee. It would be difficult to persuade importing countries to abondon such a "right". A possible course of action is that after consultations with the national administrating authority, the exporting country whose products are under investigation can bring the case to the Committee which in turn establishes an investigating panel to consider the case simultaneously with the national authority. If the panel reaches a decision that the subsidy is not distortive before the national authority, the domestic countervailing duty proceeding should be terminated. If the national authority reaches a decision of distortion first, the imposition of countervailing duties should be withheld untill the panel gives its decisions In th meantime, provisioal measures can be aplied. Such an arrangement will not unnecessarily prolong the state of uncertainty, because countervailing duty proceedings and th Code's dispute settlement proceedings are all subject to time limits.

4. According to Bárcelo, there shall be special arrangements to deal with domestic subsidies commonly used by trading nations, and countervailing duties can only be used to sanction violations of such arrangements. He also suggests the EEC approach to handle subsidy problems in the GATT context. The adaptability of the EEC approach is subject to the following considerations. First, the institutional structures of the GATT and the EEC. The GATT was built on a multilateral contract, or an international code of conduct, which regulates the rights and obligations of the contracting parties towards one another and intended to protect the private interest of each contracting party. Contracting parties only refrain from so exercising sovereignties as to adversely affect the trade interests of other countries. Such a degree of restraint on the exercise of sovereignty is not sufficient for the GATT to be a supra-national organization. The formation of a supra-national organization requires some degree of political integration which would in turn allow greater external restraints on national organizations. The EEC has more of the features of a supra-national organization. The EEC Commission's decision can preempt national legislations of member countries and the European Court of Justice can overrule the decisions of national courts. In controlling subsidies, the EEC Commission is able to review national legislations regarding subsidies before passage, and

approve or disapprove the granting of subsidies by the governments of member countries. In other words, the EEC Commission is powerful enough as to impose restraints on national sovereignties on the use of subsidies; whereas the GATT can only restrain the exercise of sovereignties from affecting trade interests of other countries. Meanwhile, control of subsidies in the EEC fashion will require a fundamental change of the GATT organizational structure which would involve the injection of political elements into a trade organization. The second consideration is the divergence in economic structures and stages of economic development as well as attitudes towards government intervention among the EEC members and the GATT contracting parties. The EEC Commission laid down general rules regarding specific types of subsidy, and the effectiveness of these general rules depends on several factors. "The Nine must either be roughly equal in terms of their developmnt; or perceive their relative inequities as not affecting their interests and ability to support general rules; or see their long run economic development as being positive and acceptable in terms of continued membership in a customs union."*2 The difficulty posed by the disparity in economic development with regard to the applicability of a general rule can be exemplified by the constant requests from the relatively weaker countries, such as the U.K. and Italy, for exceptions to the general rules. Difficulties also arise from the divergence in economic structure and this can be demonstrated by the row surrounding the Common Agricultural Policy. Meanwhile, the constant pressure exerted by Germany on the EEC subsidy control policy can explain what the divergence in attitudes towards subsdies can cause in enforcing a general rule. The magnitudes of disparity in economic structures, developments, and attitudes towards subsidies are much greater in the GATT than in the EEC context. It can therefore be expected that the adoption of the EEC approach will encounter enormous difficulties in overcoming these disparities. Even some form of agreement can be reached, it will not be so concrete as to serve as a criterion for the application of countervaling duties. Such agreement can only provide guidelines for governments in considering in which form and to what extent a subidy can be used. Whether a specific subsidy practice is in violatin of an agreement is an ex post decision to be made on a case-by-case basis. The proper forum for such a case is the Committee on Subsidies and Countermeasures rather than national administrating authorities. However, in order to reconcile with domestic pressure, simultaneous consideration by an investigating panel and national administrating authorities discussed previously is also recommended in this context.

4. The feasibility of the proposal that the injury test for countervailing domestic subsidies should be serious injury and the causation test should be important but no more important than any other cause is also doubtful. As the experience from pressing the incorporation of an injury test into the U.S. countervailing duty law teaches, it can hardly be expected that the U.S. will be persuaded to move a step further from material injury to serious injury, let along a self-initiated move by the U.S. towards that direction.

Barcelo Prposal II *3

In two more recent papers, Barcelo slightly changed his view towards countervailing duties and modified part of his proposal. Barcelo argues that subsidies in many cases are non-distortive and it is difficult to know which subsidies are distortive and which are not. Even if a given subsidy is inefficient in some acceptable sense, it would not directly harm an importing country because the subsidized imports merely allow increased consumption and improved welfare, unless they cause escape clause injury. As to the argument that subsidies are unfair trade practices, Barcelo sees no plausible way of and no reason for distinguishing between a benefit resulting from a government decision and a benefit resulting from a plentiful supply of labour. The argument of unfairness is at most vague and problematic. In so far as subsidies having the effect of causing injury to domestic industry of an importing country are concerned, Barcelo proposes that counteractions can be used only when they cause escape clause injury. Such use of safeguard action to counteract foreign subsidy practices can be on a selective basis, and no compensation to the exporting country is required. The strongest argument against this proposal and for retaining countervailing duties, as Barcelo points out, is that adoption of the proposal would encourage protectionist forces to concentrate upon and to seek to weaken the injury test or, in the case of the U.S., to eliminate presidential discretion in the current escape clause.

In the case that a country's exports are displaced by foreign subsidies, the dispute settlement scheme provided in the Subsidy/Countervailing Duty Code offers a sound basis for the development of an international consensus on whether a subsidy practice should be considered actionable. The word "actionable" does not imply "illegal" or "wrong". It is nearer to the notion of distortion as commonly agreed. The scheme also provides a good basis to pressurize a country whose subsidy practices are found actionable to remove them.

Comment

Barcelo's proposal of using discriminatory and non-compensatory safeguard action to counteract subsidies may confront the problem of its feasibility. It can hardly be expected that domestic industries would accept such a proposal. More detailed discussion on using safeguard action as a countervailing measure can be seen in the next section dealing with the Lowenfeld proposal.

As to the counterargument that countervailing duties may ease the pressure to weaken the injury test and eliminate presidential discretion, it should be noted that countervailing duties can be used as a more effective protective instrument than safeguard measures. Moreover, countervailing duties are the least appropriate instrument for easing protectionist pressure, mainly because of their damaging effects on international trade relations.

As to the use of the dispute settlement and consultation scheme to reach international agreements in regard to the determination of actionable and inactionable subsidies, the proposal presents a sound approach.

Section II: <u>Lowenfeld Proposal</u> *5

The Lowenfeld proposal is aimed at the reform of the trade laws of the U.S., but it is also suggested that the reform be carried out in other trading countries. The main part of this proposal is quoted as follows.

> " Looking first at domestic law for the United States, one proposal would be to repeal all of the various statutory remedies...concerning dumping, subsidies, unjustified trade practices, unfair trade practices, unfair import practices, escape clause relief., and replace them by a single statute to provide relief from excessive imports. If the steel industries is in trouble and needs (deserves?) help, the argument would run, why go through all the various remedies with their differing procedures, cumbersome and internationally fact finding, most of which pretend in some way to focus on the exporter, when the real concern is the displaced domestic manufacturer? Instead, under this proposal, an industry (or perhaps part of an industry) could apply for import relief upon a showing
> (i) that it was being and likely to be injured; and
> (ii) that the cause of the injury was excessive imports. "

To make this proposal workable, Lowenfeld also suggests several supplementary rules.

(1) There would be no finding of injury, when either or both of the following is found:

(a) prices in the domestic industry were rising in the relevant period;

(b) the volume of sales by the domestic industry had risen in the relevant time period.

(2) Injury should be defined along the line of escape clause relief, i.e. serios injury.

(3) Determination of injury, like the case of escape clause action, should look into utilization of productive facilities, employment and profits.

(4) Causation might be defined so as to avoid attributing to imports domestic failure resulting from domestic cause; a comparative causation standard might be built into, so that, if a slump on the domestic industry was attributable 40 per cent to increased imports and 60 per cent to reduced domestic demand, a proposed 12 per cent tariff surcharge could be set at 4.8 per cent.

(5) Such a new form of relief would focus on the injured party or industry, not on scrutiny of the exporting country or enterprise.

Lowenfeld also raises three problems which need special consideration but does not provide the answers. They are:

(1) is there a need to distinguish industries which are of national concern, such as steel or chemical industry, from those which are not?

(2) is there a need to distinguish imports threatening a highly competitive, multi-unit industry from those threatening a tightly controlled monopoly or oligopoly?

(3) ought there be some constraint on countries not to export, over

time, more than they import in order to prevent imbalance of payments between two countries? or put the question in the context of determination of injury, is there and should there be a standard of injury that goes beyond specific product and industry, and looks to countries as a whole?

In a more recent paper "Fair and Unfair: does it Matter?",*5 Lowenfeld gives a more detailed discussion on the distinction between fair and unfair trade practices in support of the proposal outlined above. He first points out that the requirement of injury in antidumping law indicates that dumping practices are not considered as malum in se but malum prohibitum. This is also true in the case of countervailing duty law regarding which there are two further supporting facts. Firstly, up to the Trade Act of 1974, the U.S. only imposed countervailing duties against dutiable goods. Secondly, in the course of the Tokyo Round negotiation, the U.S. was under pressure from European countries to incorporate an injury test into its countervailing duty law, and failed to make subsidies on production illegal per se . One may conclude from these facts that all industrial nations "are concerned about market share, import penetration, and similar terms looking into the importing, not to the exporting countries." The second point of Lowenfeld's thesis is that in actual practice, the Trigger Price Mechanism, and the Davignon Plans regarding the use of automatic antidumping duties are all illustration of how indistinct the difference between fair and unfair trade has become. This, together with international aspect of the Common Agricultural Policy and various textile arrangements, is a further manifestation of a concern about imports in a greater amount than acceptable. The third point is that under current U.S. trade laws, conditions for actions against fair and unfair imports are very similar and all of the conditions look to the importing rather than exporting countries. As to the difference in the quantum of injury, Lowenfeld recognizes that the legislative history and the popular understanding is that serious injury is a standard higher than material injury, but he perceives no clear distinction as such in the Trade Agreements Act of 1979. Finally, in regard to the GATT law, Lowenfeld finds that the term "material injury" used in the Antidumping and the Countervailing Code is not "powerfully different" from the term "serious injury" used in Article XIX.

Comment

1. Fair and Unfair : That national governments only concern about the acceptable level of imports rather than whether the increase in foreign imports results from unfair trade practices is a correct diagnosis of current trade problems. However, before entering into the conclusion that there is not much difference between fair and unfair trade laws, one has to make a close comparison of these laws. The validity of this conclusion not only affects the soundness of the theoretical foundation of the proposal but also is crucial to its feasibility. Conditions for taking antidumping, countervailing and safeguard actions are listed in the following.

Antidumping	Countervailing	Safeguard
1. dumping	subsidy	unforeseen development and concessions causing injury
2. material injury	material injury	serious injury
3. simple causation	simple causation	principal causation
4. definition of industry		

producers of like products	producers of like products	producers of like or directly competitive products
5. exception to MFN	exception to MFN	MFN
6. no compensation to exporters	no compensation to exporters	compensation or retaliation

Setting aside the first condition,i.e. dumping, subsidy, and increased imports caused by unforeseen developments and the effect of the obligation incurred under the General Agreement, I shall in the following analyze how far other conditions in the context of antidumping and countervailing duty laws differ from those in the context of safeguard law.

2. Material v. Serious Injury

The term "material injury" and "serious injury" are not explicitly defined in the General Agreement and the codes. The legislative history of the codes and common understanding is that serious injury is a standard higher than material injury. How far these two standards differ from each other would depend on national implementing legislations and interpretations by administrating authorities. In the case of the United States, the Trade Agreements Act of 1979 defines material injury as injury which is not "inconsequential, immaterial or unimportant" and in practice injury more than *de minimis* would suffice. Although the *de minimis* practice has been hardened to some extent because of the pressure from other countries, there is no consistent trend toward the establishment of a higher standard and the *de minimis* practice still can be seen occasionally. On the other hand, the Trade Act of 1974 stipulates those indicia for determination of serious injury shall be significant in degree. Interpretations of serious injury by the USITC include:

"damage or a hurt of grave or important proportion", and "an important, crippling, or mortal injury; one having <u>permanent</u> or <u>lasting</u> consequences." (emphasis added)

From the above observation, one can hardly conclude, at least in so far as the U.S. laws are concerned, that the difference between material and serious injury is indistinct. The difference between the nature of injury determination in antidumping/ countervailing duty law and that in safeguard law will probably be endorsed by the safeguard code now pending negotiation. It is proposed that the phrase "development and prospect with regard to" should be added to the list of indicia of injury. Thus, present decline in output, market share, profit and etc., will not be sufficient to establish a safeguard case, if the prospect and development of the industry concerned are still positive in those terms.

3. <u>Simple v. Principal Causation</u>

The simple causation test, as mentioned previously, has two different interpretations. The U.S. version is that dumped or subsidized imports need only be a cause of material injury; while the EEC and Canada take the position that the import in question should be the only cause of material injury,i.e. the injury caused by the import only should be material. The term "principal cause" has also been variously interpreted, and the U.S. Trade Act of 1974 defines it as " a cause which is important and not less than any other cause". In so far as the U.S. law is concerned, there is certainly a difference, which is not indistinct, between a cause of injury (possibly more than <u>de minimis</u> would suffice) and "a cause which is important and not less than any other cause".

4. <u>Like Products and Directly Competitive Products</u>

Another crucial factor in the determination of injury is the definition of industry. The larger the industry in size, the less likely a positive determination. In antidumping and countervailing duty laws, industry is narrowly defined as producers of the like products of the dumped or subsidized imports. The term "like product" means "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." In the case of safeguard law, industry is to be composed of domestic producers of the like products. When the industry is defined in terms of directly competitive products, there may have the effect of enlarging the industry to be examined. The extent to which the industry will thus be enlarged would vary with the product in question. Even if the industry is defined in terms of the like products, the definition of the like products in the case of antidumping and countervailing duties are extremely narrow. "The like products" in other contexts is variously defined and all of the definitions are broader than that in the context of antidumping and countervailng duties.

5. Most-Favored-Nation Treatment

Antidumping and countervailing duties are two exceptions to the MFN clause, and to be applied to dumped or subsidized imports causing injury to domestic industry only. On the other hand, the common interpretation of Article XIX is that safeguard measures are to be applied to all imports rather than those imports causing injury to domestic industry only.

6. Compensation

An exporting country whose exports are subject to an importing country's safeguard action should be consulted with, and through consultation, some form of compensation may be offered by the importing country. Otherwise, the exporting country can suspend the application to trade with the importing country of substantially equivalent concessions or other obligations. Countries exporting subsidized and dumped goods are certainly not entitled to such compensation.

Judging from the difference in the quantum of injury, the required causal link, definition of industry, the requirement of compensation and the application of the MFN principle, one can hardly make a clear-cut conclusion that the difference between antidumping and countervailing duty laws and safeguard law is indistinct. In the case of the U.S., the conclusion is even more difficult to make, because of the low injury standard applied in antidumping and countervailing duty administration.

2. Having discussed the theoretical foundation of the Lowenfeld proposal, I shall in the following examine its feasibility.

The Lowenfeld proposal is in essence a more radical form of the Barcelo proposal. It involves the abolition of antidumping and countervailing duty laws and maintains some of the main features of safeguard law. The main feature of the proposal is the so-called "comparative causation standard" which, together with the proportion method in calculating the level of import relief, makes the proposal different from the conventional approach to import relief. The standard implies that it is not necessary to search for the strength of the cause link between increased imports and serious injury in determining whether to take action against imports. The strength of a causal link only matters when the issue of how far a relief measure can be applied is under consideration. Under current trade laws, an importing country is able to impose import restriction up to the margin of dumping, the full amount of the margin of subsidy, or the necessary extent to remove an injury, no matter whether the import concerned is a cause, a principal cause or the only cause of the injury. The adoption of the proposal will therefore have two consequences. First, it will be easier for an importing country to take action against imports, because an investigation of dumping or subsidy is not required and the required causal link is minimal. Second, the remedy that domestic producers can obtain through the course of action proscribed in the proposal will be less than those they can obtain under antidumping, countervailing duty, and safeguard laws. For instance, in the hypothetical case where a slump in domestic industry was attributable 40 per cent to increased imports and 60 per cent to other causes none of which is a cause more important than the increased import, under current safeguard law an importing country may justifiably take safeguard action, as the 40 per cent in the present case can be regarded as principal. Under such circumstance, an import relief measure can be as restrictive as necessary to remove the serious injury rather than 40 per cent of the injury. The conditions in the hypothetocal case are in most cases sufficient for the invocation of antidumping and countervailing duty laws, save the condition of dumping or subsidy. Under these two laws, import duties can be as high as the margin of dumping or the full amount of subsidy which would normally be higher than 40 per cent of the import duties necessary to remove the serious injury. Other than these two consequences, there may be technical difficulties in determining how many per cent of the seriou injury is attributable to increased imports. Given the current legal technique, the best can be achieved is the weighing of the importance of one cause against the others. Even this would involve enormous complications, let along showing a causal link in exact percetage.

Will domestic producers of an importing country accept such a proposal at the expense of the abolition of antidumping and countervailing duty laws? Under the proposal, domestic producers would not be burdened by the condition of dumping or subsidy, but such a relief is hardly a significant one. In the case of antidumping administration, the use of pre-established target prices or costs of production as the normal value to be compared with the sales prices in the market of the importing country greatly increases the possibility of a positive determination of dumping and reduces the administrative and judicial complications that may otherwise be involved. In the case of countervailing duty administration, the illustrative lists of export subsidies and of other subsidy practices provided in the Subsidy Code would clarify the uncertainties in identifying subsidy practices. Meanwhile, in those areas like steel or petro-chemical products where countervailing duties are most frequently used, subsidy practices are common and not difficult to identify. Secondly, under the proposal, domestic producers would be faced with more stringent injury standard. As mentioned previously the difference between serious and material injury is hardly indistinct and a lawyer representing domestic producers may find the difference wide enough as to decisively influence his strategy in seeking remedy for his clients. It is also possible that national administrating authorities are more likely to render a positive determination of injury when there is already a positive determination of unfair trade practice.

Thirdly, the level of import duties that can be imposed under antidumping or countervailing duty laws is very likely higher than that can be imposed under the proposal. After weighing the possible loss and gain, domestic producers may find the proposal unacceptable.

Will national governments of importing countries accept the proposal? To them, the main concerns are whether the import restriction under the proposal shall be applied non-discriminatorily, and whether their actions against imports will be subject to compensation or retaliation. These two issues are particularly crucial because domestic pressures for protection which previously could be eased to some extent by antidumping and countervailing duties now concentrate on one legal outlet. Under such circumstances, the frequency of actions under the proposal will be greatly increased. If both the conditions of non-discrimination and compensation are maintained in the proposal, an importing government may find the proposal too costly to be acceptable. The price for the removal of these two conditions may be more stringent requirement on the quantum of injury or some other conditions, which may in turn strengthen domestic producers' objection to the proposal and may therefore be a equal deterrent to the conditions of non-discrimination and compensation for the government from accepting the proposal.

Such a proposal may be welcome by exporting countries. The abolition of antidumping and countervailing duty laws may relieve exporters from the harassement of antidumping and countervailing duty proceedings as well as the duties. The comparative causation standard can limit exporters' liabilities to injury caused by imports only. Although an exporting country may be subject to more frequent no-fault import restrictions, the number of action under the proposal only may not exceed the total number of antidumping, countervailing duty, and safeguard actions. Moreover, it can also use the right to retaliate as a lever to deter importing countries from taking actions without restraint. However, if the proposal does not accord exporting countries the right to retaliate and the MFN protection, they may hesitate to accept it.

3. Among the three issues raised by Lowenfeld for special consideration, the one regarding industries of national concern is related to the sectoral approach in solving trade problems and the issue will be dealt with in the last section.

4. The second issue concerning the difference in market structure is in essence the argument for placing more emphasis on the state of competition in the importing country in making determination of injury. The feasibility of adding such a consideration into the proposal is doubtful, as the loudest voice for protection usually comes from domestic oligopolists or monopolists.

5. The third issue relates to the argument for over-all reciprocity between two trading nations. Whether such a principle which contradicts the most fundamental principle of the GATT --- multilateralism, will be accepted by all or most of the trading nations remains to be seen. The issue is well beyond the scope of present discussion.

Section III: Hindley Proposition *6

The Hindley proposition focuses on the relationship between voluntary export restraints and safeguard actions under Article XIX. After the examination of the economics of VERs, Hindley concludes that VERs would raise the profitability of an exporting industry and its total profits will increase if certain conditions are fulfilled. The conditions are not difficult to fulfill and in many cases they will be fulfilled. Moreover, when the alternative to an VER is the emergency action under Article XIX rather than unrestricted trade, an VER arrangement will be more beneficial to the exporting industry whose profits will be reduced as a result of increased tariffs or imposition of quota (when the quota rights are distributed to importers) under Article XIX. Although the exporting country is entitled to be compensated or to retaliate under Article XIX, compensation in the case of VER is more direct and just. This is because under Article XIX compensation is usually in the form of further concessions to other exports of the exporting country while in the case of VER compensation is directly paid to the industry whose exports are restricted through increased profitability and profits.

Among various alternatives for an importing country to achieve the aim of redistributing income from trade, the VER is the most costly instrument. From an economic point of view, there will be a welfare cost attached to a subsidy policy which is directed at maintaining factors in employment in an industry in which the value of their marginal product is less than it would be were they employed elsewhere. But the subsidy is merely a transfer within the country. A tariff or a quota entails an additional loss to consumers because of the distortion caused by the tariff or quota in their perception of the opportunity cost of consuming the protected good. Adjustment assistance involves none of the above mentioned losses and the only cost is the transfer payment. Both protective and adjustment policies are all less costly than a VER. An importing country entering into a VER agreement has to forego the tariff revenue or revenue from the sale of quota rights that it would have raised if tariffs or quotas (when the quota rights are distributed to importers rather than foreign exporters) were imposed.

Although the cost of a VER is high, governments would still prefer its use. This is because governments are much more likely to use direct restriction such as tariffs and quotas rather than subsidies or adjustment assistance. Secondly, the use of tariffs and quotas for emergency action is controlled by Article XIX which requires non-discriminatory application and compensation to the exporting country affected. These two restrictions would cause political difficulties to the importing country taking Article XIX action. In terms of external political relations, the government would hesitate to accuse old-established partners of market disruption because international trade is usually regarded as an exchange of political concessions. Political difficulty also arises from negotiation of compensation with all the exporting countries of the product in issue. In terms of internal politics, offering other concessions as compensation would hurt the interest of another industry and make the protection politically costly. An VER may have the advantage of applying restriction on a selective basis and incuring less political cost as the cost of a VER falls on the consumers who are not so well organized as producers and spreads across all sectors.

With respect to the issue of whether it is necessary to eliminate VERs from international trading system, Hindley makes the following observations. First, with regard to the uncertainty as to when, in what ciraumstances and for how long a VER will be requested, the same uncertainty also exists in Article XIX actions which under current law are largely unregulated. It would be unwise to eliminate VERs on the ground of uncertainty while leaving Article XIX untouched, as exporting countries would be better-off under a system of VER. Second, it is also wrong to attribute the formation of cartels in exporting countries to VERs, because there are more plausible means for distributing quota rights created by a VER than cartelization. To eliminate VERs in order to deter cartelization in an importing country is also a misleading assertion, as there are other means, such as the U.S. Trigger Price Mechanism and the automatic application of provisional antidumping duties under the Davignon plan, available to assist cartelization. Moreover, since the cost of using VERs to assist cartelization mostly falls on the residents of the importing country, there is no reason to control VERs so as to prevent sovereign powers from imposing costs on their own residents. Third, as to the coercive elements in a VER arrangement, they will not die with the elimination of VER ; instead, they will be used to extract some other concessions, probably even more damaging to the world economy. Fourth, as far as the legality of VERs is concerned, it is more appropriate to consider them as out-of-court settlement in civil litigation rather than an arrangement outside the restrictions of GATT rules.

Basing on the above analysis, Hindley argues that any attempt to reduce the use of VER by loosening some of the conditions for the invocation of Article XIX, say, the removal of the condition of non-discrimination, would be unwise. Such a change will make importing countries less inclined to request for VERs and rely on Article XIX for protection. Thus, the distributition of world income will shift in favor of importing countries who in most cases are developed countries. Although exporting countries have the right to be compensated or to retaliate, small or weak countries may not be able to make retaliation so politically costly for an importing country to be deterred from taking safeguard action without restraint. Meanwhile, compensation under Article XIX is not so meaningful and just as that under a VER arrangement. It is also unwise for developing countries to exchange the conditions for the use of safeguard action selectively, as standards and enforcement in the GATT are not effective enough to be the sole safeguard. Fianlly, the reform of Article XIX currently under discussion should not be linked to the problem of VERs and any reform of Article XIX aiming at elimination of VERs should be rejected.

Comment

1. The Hindley proposition shows the position of VER relative to those of other means of protection. The proposition also gives a fair account of VERs in terms of distribution of world income between importing and exporting countries and between developed and developing countries in particular. The important message is that VERs are not so much of a devil as commonly perceived.

2. Despite its advantage in shifting world income in favor of exporting countries, a VER is as a distortive element in international trade as other instruments. A sound trading system would not leave a distortive element totally undisciplined. The crucial issue is therefore to find out the balancing point at which exporting countries can be appropriately compensated and the distortive effects can be reduced to the minimum possibility. The rule, as laid down by Hindley, is that elimination of VERs through changes in the conditions for invocation of Article XIX should not be allowed. What are the alternatives? One alternative is that VERs should be banned in general but there may be exceptions, and be incorporated into Article XIX as a safeguard measure. Exception to the general ban on VERs is

the use of VERs in some sensitive sectors. In those sensitive sectors like car, steel, and chemical industries which are most affected by recession and structural changes, VERs can be allowed. These are areas where protective instruments like antidumping and countervailing duties, safeguard measures are most frequently applied. Since protection and therefore distortion in these sectors are inevitable, VERs which under multilateral discipline are no more (or less)distortive than other measures and may give exporting countries just compensation is a sound alternative mechansim for protection. However, a multilateral framework must be set up to discipline the use of VERs in such a context, otherwise the use of VER would probably result in more distortion than other measures. The MFA can provide a sound model, except those sofening arrangements like the interpretation that jointly agreed departure is included in the definition of mutually acceptable solution. Such multilateral arrangements can provide a trading order which allows breathing space for importing countries to restructure their industries. For instance, under such an arrangement, the EEC can undergo its steel contraction plan without resort to various import restrictions. Multilaterally disciplined VERs are much less distortive than those VER arrangements made under the threat that failure to respond to the request for VERs would lead to imposition of high antidumping or countervailing duties. They also provide compensations to exporting countries which would not have compensation at all under the protectionist use of countervailing and antidumping duties. Meanwhile, countries participating in such multilateral arrangements shall enter into a commitment to refrain from using other protective instruments like antidumping or countervailing duties, or safeguard actions under Article XIX.

Proposals of This Thesis

Some of the proposals of this thesis have appeared in the comments on the Barcelo proposals and the Hindley proposition. There will therefore be repetition of those discussed previously in the following presentation of the proposals of this thesis.

Dumping and Antidumping

This thesis agrees with Barcelo that dumping in most cases is consistent with global efficiency and the need for antidumping law from efficiency point of view is doubtful. However, this thesis disagrees with his proposal for antidumping law reform because of its infeasibility. Arguments basing on the notion of fairness (rather than efficiency) for protection against dumped imports are particularly strong in time of economic hardship, no matter whether they can be justified on rational grounds. Thus, it is extremely d fficult, if not impossible, to carry out positive legal reforms under heavy political pressures. In stead, this thesis seeks to provide feasible means to prevent antidumping practices from moving towards a more protectionist stand. There are two approaches that can be followed: first, to remove protectionist pressures from antidumping administration, and second, to search for counterforces to offset the protectionist pressures. With regard to the first approach, several instruments can be used, including use of VERs in the case of sensitive industries, government subsidies to slow down the declining process of ageing industries, and adjustment assistance. Use of VERs for sensitive industries under a multilateral framework can place the exporting countries concerned in a stronger bargaining stand and therefore causes less distortion than use of VERs (voluntary undertakings) as a substitute for antidumping duties. This is because in the latter case, when facing the alternative of antidumping duties, the exporting countries concerned would have to accept the terms set by the importing country whose bargaining power is backed by its right to impose antidumping duties. However, in the former case, like in the case of MFA, the terms should not be lower than the flooring limits set in the international agreements. Moreover, under the proposals of this thesis, the importing country concerned should refrain from taking other protectionist action when the import under consideration is included in a multilateral VER scheme. More on use of VERs as a means to ease political pressures for protection will be discussed in the proposal regarding use of VERs as a safeguard instrument. Adjustment assistance is consistent with efficiency considerations. The effects of domestic subsidies are less direct and more permissible under the Subsidy/Countervailing duty law, and therefore their use is less disrupting than abuse of antidumping duties to the GATT legal order.

As to the search for counterforces to offset the protectionist pressure on the importing government, there are domestic as well as international forces that can be mobilized. There are the domestic cumsumers groups and the international trading community. Since consumers groups are mainly a domestic factor, it is of little concern in discussing international legal reform. International forces can be derived from two sources: international sanction and international pressures. As discussed in Chapter I of this part, the language of existing international trade laws regarding dumping, i.e. Article VI and the International Antidumping Code, is so vague that they turn out to be an endorsement of national protectionist antidumping practices. Since it is difficult to establish a technical case of violation or nullification of benefits, the feasibility of using international sanction to influence government decisions is remote. However, as the discussion regarding enforcement of GATT rules in Chapter III of Part Two points out, a more effective means to enforce international law is the formation of international pressures on countries abusing their rights or even violating GATT rules. The International Antidumping

Code is equipped with such a facility for the formation of international pressures. Namely, its supervising body, the Committee on Antidumping Practices, and the regular meetings of its signatories. In such meetings, countries can present and discuss their views regarding other countries' practices. Through group discussions, international pressures can be formed. There may be cases where a country is prevented from bring its case to international attention when facing either political or economic coercision from the country abusing antidumping duties. The Committee should therefore be equipped with a surveillance machinery and be empowered to "prosecute" or to bring the case to the regular meetings of signatories.

Subsidies and Countervailing Duties

This thesis recognizes the complexities of subsidies and considers countervailing duties as not an appropriate instrument in offseting subsidy effects. This is because whether a subsidy practice is objectionable is to be determined according to the international consensus by an international body, and countervailing duties are solely administered by national authorities according to their own judgements. This thesis also doubts the feasibility of applying the EEC model to regulation of domestic subsidies, because of the differences in institutional structures, and divergences in levels of economic development as well as economic structures of member countries, of the EEC and the GATT.

In order to reconcile the need for removing decision-making process regarding, in Barcelo's term, the "actionability" of a subsidy to an international body , and the right to use countervailing duties, this thesis proposes a simultaneous decision-making scheme. Under the scheme, a national authority shall notify the Committee on Subsidies and Countervailing Measures upon initiation of a countervailing duty investigation. The Committee will then upon request of the exporting country concerned appoint a panel of experts to investigate the subsidy in issue simultaneously with the national authority. If the national authority reaches a positive determination regarding the existence of an objectionable subsidy first, it shall suspend its proceeding untill the panel reaches its determination. In the meantime, provisional measures can be used. If the panel's decision is negative, the national authority shall terminate its proceedings and provisional measures immediately. Both the national authority and the panel should complete their investigation within a certain time limit. Such a decision-making pattern has the advantage of providing national governments an exist from the dilemma where both domestic industries and foreign governments exert irresistable pressures on it. Such a simultaneous investigation can also prevent use of countervailing duties as a protective instrument by adding international factors into the decision-making process. Thirdly, since the case is considered by the panel and the national authority simultaneously, exporters or importers would not suffer from the prolonged uncertainty that may be resulted from conventional dispute settlement proceedings. Under the conventional scheme,the exporting country is obliged to make efforts to reach a mutually acceptable solution before complaining to the GATT. The time period needed to reach a final decision on the legality (or actionability) of a subsidy is the total of the time needed for determination of subsidy and injury by national authorities, the time for consultation, and the time for the Committee to investigate the subsidy in question. Fourthly, such a simultaneous investigation scheme would increase the opportunity for GATT panels to make decisions on the actionability of various subsidies. The compilation of these decisions is a development process of common law of subsidies. These decisions can also provide guidance for governments in using subsidies as policy instruments. Such a legalistic approach would not significantly undermine the operation of the basic dispute settlement mechanism of the

GATT, i.e. negotiation of a mutually acceptable solution through consultation. This is because if the exporting country sees the feasibility of reaching a mutually acceptable solution,e.g. it may feel its subsidy practice is likely to be actionable,or for political reasons it is willing to accept whatever it can achieve in the negotiation, it would not request the Committee to set up an investigating panel. If it sees no such feasibility before the national authority or the panel has reached its decision, because it is confident that its subsidy is not actionable, it can always enter consultation after a positive determination regarding the existence of an actionable subsidy either by the panel or the national authority has come out.

Safeguards and VERs

This thesis does not accept the feasibility of using a safeguard system as the only protectionist instrument. This is because domestic protectionist pressures would not accept a safeguard system at the expense of the abolition of antidumping and countervailing duty law. Even a sofened safeguard system as proposed by Lowenfeld would not be sufficient to fulfill the needs of domestic protectionist elements. However, this thesis believes that a well designed safeguard system, involving greater use of multilaterally disciplined VERs, can reduce the pressures on antidumping and countervailing duty administration. To improve the flexibility of the current safeguard system, this thesis proposes a two-track safeguard system. The first track is based on the general safeguard system under Article XIX and the Draft Code. This system should follow the following principles. First, the right to retaliate against a safeguard action should not be weakened, i.e. those provisions in the Draft Safeguard Code imposing conditions on the right to retaliate should be eliminated. Second, the principle of non-discrimination should be universally applied and no exceptions should be allowed. The combined application of the right to retaliate and the principle of non-discrimination is the best protection against abuse of safeguard actions. Third, the causation between the increase in imports and the serious injury should not be lower than principal causation. The above mentioned three principles would harden the general safeguard system and therefore can minimize the distortive effects of safeguard actions. Fourth, VERs should be incorporated into the general safeguard system and be given the priority as a safeguard instrument. Such an arrangement would allow exporting countries, especially developing countries, to be compensated automatically without depending on their political or economic strength in bargaining for compensation from, or retaliate against, the importing country.

Since under the general safeguard system as proposed above, it is difficult to take safeguard action, its acceptability to domestic protectionist elements would depend on whether there exists an outlet for the assertion of protectionism. Most of the protectionist forces are from those sectors most affected by recession and structural changes. These sectors include steel, auto, textile, other labour-intensive, and to some extent chemical industries. This thesis therefore proposes a sectoral safeguard system to be applied to these sensitive industries as the second track of the two-track safeguard system. Such a sectoral safeguard system is similar to the dual safeguard system under the MFA, saving those sofening clauses that have greatly weakened the MFA. This sectoral system would consisit of two sub-systems, one similar to Article 3, the other to Article 4, of the MFA. The Article 3-style system would allow discriminatory application of safeguard measures and imposes no obligation of compensation and provides no right to retaliate. However, an importing country intending to take safeguard action is obliged to demonstrate the existence of serious injury and safeguard actions shall be subject to limits regarding product coverage, duration, restraints on import volumes and annual liberalization rates. The Article 4-style safeguard system would allow countries to enter bilateral arrangements under a multilateral framework. This means such bilateral arrangement should be subject to the minimum terms set in the multilateral negotiations, and surveillance of an international governing body. The "jointly agreed reasonable departure" clause would under no circumstances be allowed to appear in the proposed sectoral safeguard system. Countries participating in such a sectoral arrangement should agree to refrain from taking safeguard action against imports of products covered by the arrangement outside its framework. Moreover, in so far as those products covered by a sectoral system is concerned, there shall be a commitment that other protective instruments like antidumping or to some extent countervailing duties would not be used.

The above mentioned sectoral system has the practical problem of which sector is eligible for such a safeguard arrangement. The problem is to be solved by both economists and politicians. The economists' task is to conduct a careful research on which sector is in secular transition and most volunerable to recession. The GATT has gathered a group of economists and it can set up a working party to examine the eligibility of a sector for special arrangements. The working party will also have to establish criteria for assessment of eligibility. Secondly, the working party has to make differentiation between conditions and nature of those eligible sectors and therefore provide basis for legal differentiation with regard to the maximum extent of restraints on trade volume, and the maximum duration, of safeguard measures , and the minimum annual growth rate. If a sector is relatively slower in adjusting to secular changes, and in more serious conditions,the maximum re traints can be set at a higher level, duration can be lengthened, and the minimum growth rate can be lower, and vice versa. Thirdly, the working part has to develop a technique to define a sector for such special arrangement. The definition should take into account the backward as well as forward linkages of the sector in question to other sectors and should be able to single out a sector most in need of secial arrangements from a chain of integrated sectors. The definition should also be so designed that it would not seriously affect the competitive relation in other sectors. After economists put forward their plan, it is politicians who should get together and negotiate on the basis established by the economists' plan to reach a politically acceptable framework. As to the criteria for assessment of eligibility, it is essential for national governments to enter a commitment that the criteria once accepted by negotiating parties will not be weakened in the future when domestic pressures become heavier.

Proposals of this thesis may in some points appear conciliatory to protectionist forces. However, they are the second-best alternatives because of the impossibility of attaining more positive improvement under current economic climate. The proposals on antidumping and countervailing duty law reform can prevent further protectionist application of these laws with the possibility that through multilateral efforts there may be positive improvement in economic upturns. The two-track safeguard system seperates sensitive industries from other industries not so much affected by structural changes and recession and treats them differently. Such a device would on the one hand tighten the general safeguard system and therefore reduce distortion that may be caused by safeguard actions. On the other hand, it allows more flexible treatment for sensitive sectors and thus increases the acceptability of the tightened general safeguard system to protectionist forces.

The sectoral scheme as proposed would not cause more distortion than unregulated use of VERs and abuse of safeguard actions under a single-track safeguard system, or a general safeguard system imposing condition on the application of the principle of non-discrimination and the right of retaliation. Most importantly, the two-track safeguard system could encourage importing countries to take safeguard actions within a legal framework and therefore greatly reduce distortions resulting from uncertainties as to under what circumstances and when imports would be met with import duties or restrictions. In addition, the two-track safeguard system also provides a politically neutral means of compensation through the use of VERs.

Finally, this candidate wishes to re-emphasize that the proposals as presented above are aimed at improving legal orders in time of economic hardship. The political relaity in economic downturns limits this candidate's ambition to search for more radical reforms. When the recession is over and structural changes can proceed more smoothly and entail minimal dislocation cost , there will certainly be a need for more radical reforms. Barcelo's proposal shows the direction for legal reform in antidumping law. Namely, antidumping law is to be abolished or the injury test shall take into account the competitive effects of a dumping practice. Countervailing duties are to be replaced by international sanction according to the decisions of the international trade forum. Most importantly, the sectoral safeguard system is to be gradually phased out and the general safeguard system as proposed in this thesis shall be the sole remedy for import-caused social sufferings.

<u>Footnotes</u> (Part Three, Chapter I)

1. Exterritorial application of domestic antitrust law is possible but rare. It is rare because frequent use of domestic antitrust law to penalize arrangements between foreign producers would arouse antagonism of foreign governments.

2. D. Dale, 'Anti-dumping Law in Liberal Trade Order', pp. 20-27

3. For instance, see <u>European Communities' Refunds on Exports of Sugar</u> , BISD 26S/290

4. D. Robertson, 'Fail Safe System for Trade Liberalization', pp.26-7

5. Article 1, the MFA, BISD 21S/3, BISD 24S/5

<u>Footnotes</u> (Part Three, Chapter II)

1. J.J. Barcelo, "Antidumping Laws As Barriers to Trade --- The United States and the International Antidumping Code", 57 Cornell L.R. pp.491; "The Antidumping Law: Repeal It or Revise It", 1 Michigan Year Book of Int'l Law (1979) pp.227; "Subsidies and Countervailing Duties ---Analysis and A Proposal", Law & Policy in Int'l Bus. vol.9:779 (1977)

2. S.J. Warnecke, "The European Community and National Subsidy Policies", in S.J. Warnecke ed., 'International trade and industrial Policies', p. 166

3. J.J. Barcelo, "The Two-Track Subsidies Code --- Countervailing Duties and Trade Retaliation", in J.Quinn & P. Slayton eds., "Non-Tariff Barriers after the Tokyo Round', "The Injury-Only Test and Actionable Subsidies", to be published.

4. A.F. Lowenfeld, 'Public Control on International Trade', pp. 367-371

5. 13 Cornell L.J. (1980), p.205

6. B. Hindley, 'Voluntary Export Restraints and the GATT's Main Escape Clause'; "Voluntary Export Restraints and Article XIX of the GATT", in J.Black and B. Hindley eds., 'Current Issues in Commercial Policy and Diplomacy'.

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Agreement on Government Procurement, BISD 26S/33

Agreement on Interpretation and Application of Articles VI, XVI and XXIII (MTN Subsidy/Countervailing Duty Code) BISD 26S/56

Arrangement Regarding Bovine Meat, BISD 26S/84

Agreement on Implementation of Article VII-- Protocol to the Agreement on Implementation of Article VII, BISD 26S/116, 151

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Australia -- Subsidy on Ammonium Sulphate, GATT Basic Instruments and Selected Documents (hereafter BISD) Vol.II,p.188

Belgium-- Income Tax Practices, BISD 23 Supplement, p, 127

Canada-- Withdrawal of Tariff Concessions, BISD 26S/42

EEC-- Minimum Import Prices for Processed Fruits and Vegetables, BISD 25S/68
E

EEC-- Measures on Animal Feed Proteins, BISD 25S/49

EEC-- Refunds on Exports of Sugar, BISD 26S/290

France-- Assistance to Exports of Wheat and Flour, BISD 7S/46

France-- Income Tax Practices, BISD 23S/114

Germany Fed. Rep. of -- Treatment of Imports of Sardines, BISD 1S/53

Germany Fed. Rep. of -- Import Duties on Starch and Flour, BISD 3S/77

Italy-- Discrimination against agricultural Machinery, BISD 7S/60

Netherlands-- Income tax Practices,BISD 23S/137

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