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THE GATT BALANCE OF PAYMENTS SAFEGUARD PROVISION: ARTICLE XII

COMMITTEE ON FINANCE
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The GATT Balance of Payments Safeguard Provision: Article XII

Article XII of the General Agreement on Tariffs and Trade (GATT) permits a contracting party to the GATT to restrict the quantity or value of imports to safeguard its external financial position and its balance of payments under certain conditions.[1] The criteria for use of import restrictions by a Contracting Party are that they shall not exceed those necessary:

(i) to forestall the imminent threat of, or to stop, a serious decline in its monetary reserves, or

(ii) in the case of a Contracting Party with very low monetary reserves, to achieve a reasonable rate of increase in its reserves.

The Role of the International Monetary Fund (IMF)

Article XV provides that, in cases involving problems concerning monetary reserves, balance of payments or foreign exchange arrangements, the Contracting Parties shall consult fully with the IMF and shall, in such consultations, accept all findings of statistical and other facts presented by the Fund relating to these monetary questions. In reaching a decision in cases involving the criteria for use of import restrictions under Article XII, the Contracting Parties are required by Article XV to accept the determination of the Fund as to what constitutes a serious decline, a very low level, or a reasonable rate of increase of reserves, and as to the financial aspects of other matters covered in consultations in Article XII cases.

Notwithstanding the requirement to "accept" the findings of the Fund on monetary and financial matters in Article XII situations, Article XV specifically recognizes that the "final decision" concerning whether the criteria of Article XII have been met rests with the GATT Contracting Parties. The relationship between the GATT and the Fund in this area has been described as follows:

> The over-all "final" decision as to whether and to what extent a Contracting Party's import restrictions are necessary, and the over-all considerations concerning the commercial effects of such restrictions, are exclusively in the province of Contracting Parties, although in reaching such "final decision" the determination of the Fund will be, no doubt, a very weighty element. (IMF, 2 *Staff Papers*, 450, 1951)

[1] This paper does not address itself to Article XVIII. 2, 6 which permits developing countries to apply quantitative restrictions for balance of payments purposes, in light of the high demand for imports likely to be generated by their economic development programs.

Various Contracting Parties to the GATT have on occasion viewed the Fund role as being very narrow and confined essentially to statistical findings as to a Contracting Party's balance of payments and reserve position. This view was expressed by some countries, for example, during the discussions of whether the U.S. surcharge was appropriate.

Surcharges and Article XII

Article II justifies the use of quantitative import restrictions that otherwise would be prohibited by Article XI when necessary for balance of payments purposes.

Several countries have resorted to import surcharges or import deposit schemes rather than quotas in situations which they considered met the balance of payments criteria for recourse to Article XII. In some of these cases, the country imposing the surcharge obtained a GATT waiver of its Article II obligations not to increase bound rates of duty. In each case the surcharge has been tolerated by the Contracting Parties although in some instances the report of the Working Party examining the balance of payments measures has expressed the view that the surcharge was inconsistent with the country's Article II obligations.

The problems that have been brought before the Contracting Parties under Article XII have not proved susceptible to easy solution. Generally cases have been handled on an ad hoc approach as is illustrated in the following cases.

French 1954 Case

In 1954, France adopted a special temporary import surcharge on certain imports. In response to a complaint filed by Italy against this action, the Government of France explained that the import tax was intended to serve as a temporary and transitional device to facilitate removal of quantitative import restrictions that had been imposed pursuant to Article XII. The Contracting Parties, in a decision taken in 1955, concluded that, whatever the motivation of the tax, it increased the incidence of duties beyond the rates bound under Article II and that the situation justified resort by affected countries to the compensation and retaliation provisions of Article XXIII. France agreed to remove the import surcharge as soon as possible and did so on August 10, 1957. (France replaced the surcharge with a system of import levies and export subsidies, which was later removed.) No action was taken by other countries.

Canadian 1962 Surcharge

On June 24, 1962, Canada imposed an import surcharge on the ground that such action was necessary to safeguard Canada's external financial position and balance of payments. A GATT decision of

November 15, 1962 expressed regret that the Canadian Government found it necessary "to introduce temporary measures inconsistent with Article II of the General Agreement" and recommended that the remaining surcharges be removed expeditiously. No waiver was either requested or granted, and the decision referred only obliquely to Article XII ("Having . . . heard the Canadian Government's explanation of the reasons why it took action through the introduction of temporary import surcharges rather than through the introduction of alternative measures. . . .") Canada removed the import surcharges on March 31, 1963.

United Kingdom 1964 Surcharge and 1968 Import Deposit Scheme

The largest trading nation to resort to an import surcharge during the 1960's was the United Kingdom. Article XII was invoked by the United Kingdom on October 27, 1964 with the recognition that this provision assumed that quotas and not a surcharge would be used. The GATT established a Working Party to consult with the British. The Working Party report stated that it was not disputed that bound rates were increased by the United Kingdom inconsistently with its GATT Article II obligations. No other GATT action was taken. The United Kingdom removed the surcharge on November 30, 1966.

On November 27, 1968, the United Kingdom imposed an import deposit scheme. A Working Party was formed to examine the United Kingdom's measure. It concluded that the deposits were not more restrictive than measures which the application of the provisions of Article XII permits. No other action was taken. When the United Kingdom terminated its import deposit scheme on December 4, 1970, the Working Party considered its work terminated. The two British cases indicate clearly that the GATT membership has been willing to accept special trade measures (without a waiver) as an alternative to quotas.

French 1968 Measures

The above cases have not been the only examples of the use of trade measures other than quotas for balance of payments reasons. In July 1968, following major civil disturbances, France cited the language of Articles XII, XIX (escape clause) and XXIII (in a novel reference to what is a complaint provision rather than a remedial clause to be used in economic difficulties) to justify the imposition of import quotas and the granting of export rebates on certain products as a partial compensation for wage increases.

A Working Party was established to examine the measure. Certain members of the Working Party expressed the view that given the reserve position of France, the necessary balance of payments need had not been demonstrated. There was particular objection to the export subsidy related to wage increases, which some Working Party

members contended might prove an unfortunate precedent. There was agreement among the developed countries represented (other than France) that the measures were not measures permitted by Article XII. France announced the progressive elimination of the import restrictions in October 1968, and the reduction of the subsidy. The subsidy was eliminated in January 1969. The GATT made no decision on the French action.

The United States, as required by domestic law, in August 1968 imposed countervailing duties on dutiable French imports into the United States which benefited from the new French subsidy.

United States 1971 Surcharge

On August 15, 1971, the United States imposed an import surcharge for balance of payments reasons. The United States did not seek to justify its measure under any particular GATT Article but stated that it felt itself entitled under Article XII to apply quantitative restrictions on imports—a harsher action than the surcharge—and cited the precedents of use of other measures. A Working Party was formed to consider the U.S. measure. The countries (other than the United States) which were members of the Working Party expressed the view that the surcharge raised tariff rates above bound levels in violation of Article II of the GATT. They also held that the surcharge, as a trade restrictive measure, was inappropriate given the nature of the United States balance of payments situation and the undue burden of adjustment placed upon the import account with consequent serious effects on the trade of other Contracting Parties.

The United States terminated the surcharge effective December 20, 1971.

Danish 1971 Surcharge

On October 21, 1971, Denmark imposed a temporary import surcharge scheduled to terminate in staged reductions by April 1, 1973. Denmark did not claim that an import surcharge was explicitly covered by any provision of the GATT but that its action had been within the spirit of Article XII and that quantitative restrictions would have had a more serious effect on other countries. The Working Party noted that to the extent that it raised the incidence of customs charges beyond the maximum rates bound under Article II, the surcharge was not compatible with the provisions of the General Agreement. The membership was divided as to whether the surcharge was appropriate.

Amendment of Article XII

A dilemma does exist between Article XII of the GATT and the use of surcharges and other nonquota trade measures by Contracting Parties in balance of payments emergencies. The drafters of the

GATT clearly had quotas in mind in the article, perhaps because they are the hardest trade measures to put into effect and because they were the device most commonly used when the GATT was drafted. However, it has become less and less feasible as time passed, for administrative and other reasons, to establish quota systems during balance of payments emergencies. When countries have resorted to trade measures in balance of payments emergencies, they have found import surcharges or deposits more acceptable because they are less onerous, and more practical. In addition, countries have favored use of surcharges rather than quotas since the former are less trade diverting, less likely to discriminate among domestic importers and among foreign suppliers, and thus politically more acceptable at home and abroad.

Article XII should be amended to reflect the current collective judgment of GATT members by explicitly allowing trade measures other than quotas to be resorted to for balance of payments reasons. Although, generally, governments recognize the extreme severity of quotas and the stigma attached to their use and are reluctant to use them, it is important that the agreed rules be workable, and authorize measures which are most acceptable and economically justifiable.

It has been argued that opening Article XII for amendment could have results adverse to U.S. interests and those of world trade generally. To revise Article XII to enumerate such nonquota restrictive measures as import surcharges and deposit schemes as acceptable balance of payments measures would make their use more respectable and countries might be likely to resort to them more frequently. The ability of the United States and other GATT Contracting Parties to control or modify their imposition and duration through GATT pressure could be lessened.

On the other hand, on the economic issues involved, surcharges are preferable because they do not isolate a country from the forces of international competition as quotas do and are therefore less objectionable than quotas.

A suggested alternative has been that consideration might be given to pressing for resort to waivers under Article XXV where trade measures other than quotas are employed. It has been urged that this approach would have the advantage of making resort to trade measures other than quotas subject to the approval of and conditions imposed by the Contracting Parties. However, the application of Article XII procedures whenever balance of payments measures have been taken can offer the GATT Contracting Parties a measure of control at least equal to the more formal waiver procedure.

At the meeting of the International Monetary Fund in September, 1972, the United States proposed a variety of changes in the rules governing the operation of the international monetary system. As stated by Secretary Shultz, "if trade controls are permitted temporarily in extreme cases on balance of payments grounds, they should be in the form of surcharges or across-the-board taxes." These and other changes in rules are currently under discussion in the IMF's Committee of 20.

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