

MASTER FILES
ROOM C-525

0440

IMF WORKING PAPER

© 1992 International Monetary Fund

This is a Working Paper and the author would welcome any comments on the present text. Citations should refer to a Working Paper of the International Monetary Fund, mentioning the author, and the date of issuance. The views expressed are those of the author and do not necessarily represent those of the Fund.

WP/92/94

INTERNATIONAL MONETARY FUND

Policy Development and Review Department

The European Community's Trade and Trade-Related Industrial Policies

Prepared by Miranda Xafa, Roger P. Kronenberg and Joslin Landell-Mills*

Authorized for distribution by Margaret R. Kelly and Naheed Kirmani

November 1992

Abstract

This paper examines the objectives and instruments of trade policy in the European Community (EC) from 1987 until mid-1992. It reviews the Community's institutional setting and policy environment as background to recent trends in EC trade policies and trading arrangements. A discussion of key issues and developments in the internal market program and its interactions with the Uruguay Round of multilateral trade negotiations is followed by a review of the main issues underlying trade disputes with third countries and trade-related industrial policies.

JEL Classification Number:

F14

* We wish to thank Christine Hörbinger and Peter Uimonen for research assistance. Many thanks also to Clements Boonekamp, Helen Junz, Margaret Kelly, Patrick Low, Julius Rosenblatt and numerous colleagues in the Policy Development and Review and the European I Departments. The authors are responsible for any remaining errors.

Contents

	<u>Page</u>
I. Introduction	1
II. Institutional Setting, Single Market, and Uruguay Round	1
1. Institutional Setting	1
2. The Single European Market Program	3
a. Background issues	3
b. Implementation of White Paper	6
3. Interactions with Uruguay Round	14
III. Trade Policy Developments	16
1. Policy setting and external environment	16
2. Instruments of trade policy	17
3. Recent trends in trade policies	18
a. Voluntary export restraints	18
b. Article 115 authorizations	19
c. Antidumping	19
d. Rules of origin	21
e. Agricultural policies	22
4. Trade agreements	26
a. European Free Trade Association (EFTA) and the EC	26
b. Association and Cooperation agreements	28
c. Relations with the former Council on Mutual Economic Assistance (CMEA) and East European Countries	30
d. Lomé Convention (ACP preferences)	32
e. GSP scheme	33
IV. Recent Trade Disputes	34
1. Disputes involving EC trade practices	34
2. Disputes involving the practices of the EC's trading partners	38
V. Industrial Policy Developments	41
1. Statutory provisions on competition	41
2. Implementation of EC competition policy	43
3. Survey of state aids in the EC	45
VI. Summary and Conclusions	47

Appendix I: Political Agreement on CAP Reform	52
---	----

Text Tables

1. European Community: Share in World Trade	57
2. European Community: Level and Direction of Trade	58
3. EC: Voluntary Export Restraint Arrangements, March 1989	59
4. European Community: Authorization of Article 115 Actions, 1980-91	60
5. EC: Antidumping and Countervailing Investigations, 1983-88	61
6. European Community: Antidumping Investigations Under "Screwdriver" Legislation	62
7. European Community: European Agricultural Guarantee and Guidance Fund--Guarantee Section, Expenditures by Sector, 1980-91	63
8. European Community: Target Prices for Selected Commodities, 1980/81-1990/91	64
9. European Community: Average Increase in Common Agricultural Prices, 1985/86-1990/91	65
10. EC, Japan, United States: Producer Subsidy Equivalents (PSEs)	66
11. EC: Total Volume of State Aids and National Aids by Sector and Function	67
12. EC: Degree of Subsidization in Selected Sectors	68
13. EC: National State Aids by Type	69

Charts

1. Shares of EC and World Trade, 1991	2a
2. European Community: Number of Voluntary Export Restraints	18a

<u>References</u>	70
-------------------	----

Summary

This paper examines the trade policy objectives and instruments of the European Community (EC) from 1987 to mid-1992. The internal market program, aimed at a single market in goods, services, and factors of production by the end of 1992, will give a further boost to intra-EC trade. The EC's external trade regime after 1992 is still evolving, but efforts to replace national restrictions with EC-wide measures may in some instances lead to continued reliance on managed trade.

There is considerable scope for trade and domestic support policies in the EC to accelerate structural reform. The EC's external trade regime is characterized by relatively low industrial tariffs, but also relies heavily on nontariff measures as instruments of protection in selected sectors (such as agriculture, textiles and clothing, and automobiles). The Common Agricultural Policy reforms agreed upon in May 1992 are a positive step toward reducing distortions in agriculture but will need to be strengthened over the longer term if such distortions are to be eliminated. EC competition policy has been more strictly enforced since 1985, and state aids are being subjected to greater scrutiny. The outcome of the Uruguay Round will also be instrumental in shaping the EC's external regime after 1992.

An important aspect of the EC's external regime is the extensive network of preferential and nonreciprocal trade arrangements. Such links are being strengthened further, particularly with regard to the European Free Trade Association and Eastern and Central Europe, as more countries seek to participate in the benefits to be derived from the single market program.

I. Introduction

This paper examines the trade policy objectives and instruments of the European Community (EC) from 1987 until mid-1992. 1/ Section II discusses the institutional setting, including the Single European Act and the program to complete the single market, and highlights the interactions between the single market program and the Uruguay Round. Section III reviews the policy setting and external environment as a backdrop to a review of trends in the EC's trade policies and trading arrangements. Trade disputes between the EC and its trading partners are covered in Section IV. Section V reviews developments in trade-related industrial policies. Finally, Section VI summarizes the main themes and conclusions of the text. 2/

II. Institutional Setting, Single Market, and Uruguay Round

1. Institutional setting

The EC was established by the Treaty of Paris (1951) and the Treaties of Rome (1957). 3/ The original six EC members 4/ were later joined by Denmark, Ireland, and the United Kingdom in 1973, Greece in 1981, and Portugal and Spain in 1986. 5/ The twelve EC countries accounted for two fifths of world trade in 1991 (Chart 1 and Table 1). Excluding intra-EC trade, the EC accounted for almost one sixth of world trade and its imports from nonmembers were higher than those of the United States. As of June 1992, seven countries had applied to join the EC: Malta, Cyprus, Turkey, and four EFTA members (Austria in July 1989, Sweden in July 1991, Finland in March 1992, and Switzerland in May 1992).

1/ The paper builds upon the coverage of EC trade issues in Issues and Developments in International Trade Policy, IMF World Economic and Financial Surveys (Washington, 1992). EC members are Belgium, Denmark, France, Germany, Greece, Ireland, Italy, Luxembourg, the Netherlands, Portugal, Spain, and the United Kingdom.

2/ It should be noted that the term "country" used in this paper does not in all cases refer to a territorial entity that is a state as understood by international law and practice. The term also covers some territorial entities that are not states but for which statistical data are maintained and provided internationally on a separate and independent basis.

3/ The EC comprises three Communities: the European Coal and Steel Community (ECSC), governed by the Treaty of Paris, and the European Economic Community (EEC) and the European Atomic Energy Community (EURATOM), governed by the Treaties of Rome. The institutions of the three Communities were merged in 1967 and are henceforth referred to as the European Community (EC).

4/ Belgium, France, the Federal Republic of Germany, Italy, Luxembourg and the Netherlands.

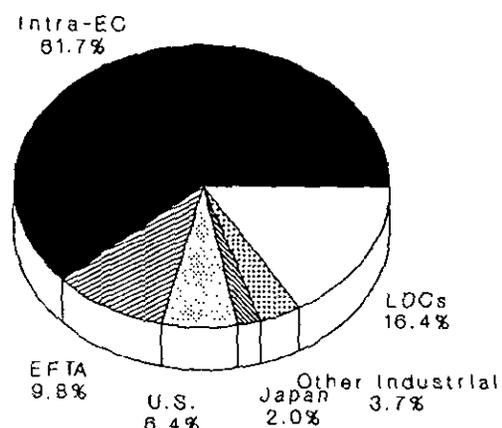
5/ The former German Democratic Republic was absorbed in the EC upon its unification with the Federal Republic of Germany.

The institutional structure of the Community consists of the European Council (of heads of state and the President of the Commission), the EC Commission, the Council of Ministers, the European Parliament, and the European Court of Justice, which constitute the administrative, legislative, and judicial branches of the EC. The Commission implements Community policy, ensures that EC treaties and amendments are carried out, draws up the budget, and proposes legislation to the Council. The Council is the final decision-making body. The Presidency of the Council of Ministers rotates among the EC member countries on a semiannual basis. The European Parliament, elected by popular vote, has supervisory powers over the Commission and is responsible for final approval of the EC budget, although it has limited power to amend it. The budget finances the EC's common policies, notably the Common Agricultural Policy (CAP), as well as EC regional and social programs, using revenues from the common external tariff and contributions paid by Community members. The Parliament acquired the power to reject or amend Council decisions pertaining to the unification of the EC market under the Single European Act of 1987. The Court of Justice, through dispute settlement and advice, interprets EC treaties and enforces Community law. The EC is not a legal member of the GATT; but by convention represents the member states and speaks on their behalf. (The EC is, however, a signatory of several of GATT codes.) Within GATT the EC is represented by the Commission which has jurisdiction over trade.

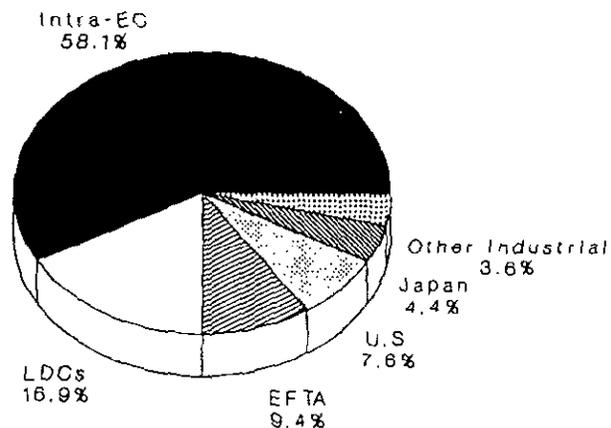
Besides establishing a customs union, the EEC Treaty provided for a common market permitting the free movement of capital and labor within the Community. Customs duties and quantitative restrictions on intra-area trade were progressively phased out over the 10-year period to mid-1968. Progress in liberalizing factor movements within the Community, however, has been slower. New impetus to this objective was provided by the Single European Act, which came into effect in July 1987 and represented the first major revision of the EEC Treaty. The Act paved the way for a fully unified EC market by end-1992, with no impediments to the movement of goods, services and factors of production. In December 1991, with the Treaty on European Union agreed at Maastricht--the second major revision of the Treaty of Rome--the EC Council agreed on steps toward monetary, economic and political union, and in February 1992 the final version of the Treaty was signed. The European Union Treaty must be ratified by the member states' national parliaments by the end of 1992. The Maastricht Treaty sets out a schedule for the adoption of a single European currency, the Ecu, by 1999; lays the foundations of a common security and defense policy; and provides for broader Community authority on the environment, health, research, networks, culture, and industrial and social policy. It offers European citizenship to EC nationals and grants the European Parliament greater powers. The Treaty does not make provision for the accession of new member states. Issues related to the Maastricht Treaty and its ratification have been the subject of intense public debate within (and outside) the EC in recent months.

Chart 1

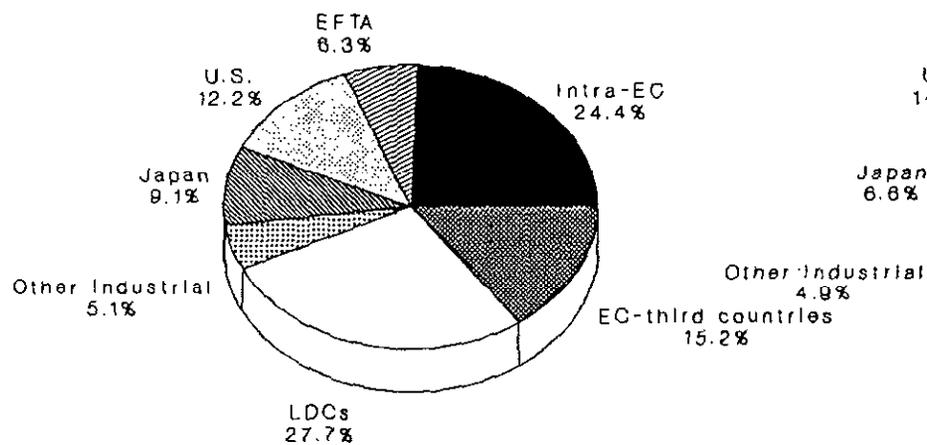
Shares of EC and World Trade (1991)



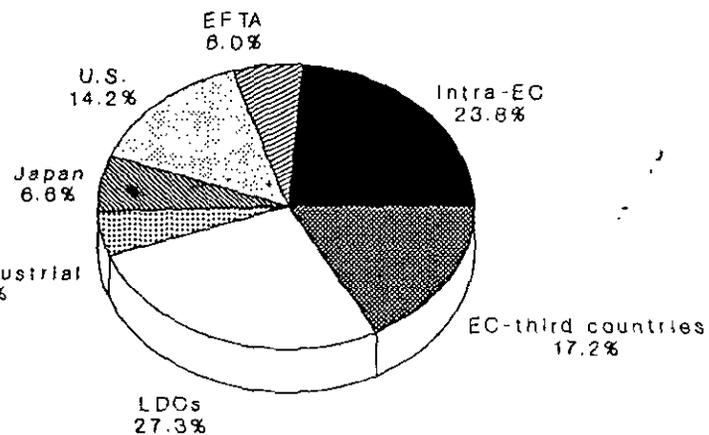
EC(12) Exports



EC(12) Imports



World Exports



World Imports

IMF, Direction of Trade

2. The Single European Market Program

a. Background issues

The Treaty of Rome identified the removal of obstacles to the free movement of goods, services, labor and capital as one of the principal objectives of the EC. 1/ Market segmentation within the EC has long been identified as an obstacle to the expansion of potential output. It raises the cost of production by distorting resource allocation, preventing the achievement of economies of scale and the adoption of cost-reducing technologies, creating monopoly rents, and imposing administrative costs. Early efforts focused mainly on obstacles to trade in goods, leading to the elimination of all internal customs duties and the full implementation of the common external tariff by 1968. Despite these important achievements, segmentation in goods markets persisted for a variety of reasons, including differences in national standards, time-consuming border formalities, discriminatory government procurement practices, national trade restrictions vis-à-vis non-EC countries, and other regulatory impediments to cross-border market entry and competition. Impediments to trade in services were even more widespread, given the virtual absence of rules and disciplines, whether multilateral or EC-based, governing such trade. National monopolies in the transportation and telecommunications sectors, along with widely different regulatory regimes in the financial service industries, gave rise to further serious trade impediments.

The first major step towards the creation of a truly unified internal EC market was the adoption by the EC Council in 1985 of the Commission's White Paper on the Completion of the Internal Market. This contained proposals to remove all physical and regulatory barriers to the free movement of goods, services, and factors of production within the Community by the end of 1992. 2/ The introduction of the paper's 300 proposals (later revised to 282 and still later expanded to include energy and an energy tax) was assisted by the Single European Act, which came into force on July 1, 1987. Implementation of the Act required agreement of the EC Council on each individual proposal and, in most cases, their incorporation--or "transposition" in national legislations. To facilitate the adoption of the proposals, the Single European Act amended the EEC Treaty by extending the areas in which decisions could be adopted by simple or qualified majority. 3/

1/ Article 223 of the Treaty of Rome allows a member to take measures "necessary for the protection of the essential interests of its security", including trade in arms, ammunition and war material, which were thus excluded from the Community's market liberalization.

2/ EC Commission (1985).

3/ A qualified majority is defined as 54 out of 76 weighted votes by the EC Council. Unanimity was still required in decisions pertaining to harmonization of indirect taxation and free labor mobility within the Community.

As of June 1992, over 90 percent of measures needed to complete the single market were in place. Agreements on insurance, public procurement, air transport and maritime cabotage were in their final phases. However, only one of the proposals for abolishing border controls had been submitted to the Council. Over 300 items are still theoretically subject to border checks, and only four countries--Luxembourg (May 1992), Spain and Portugal (April 1992) and France (1991) have ratified the Schengen Agreement, which covers the free movement of people within the EC as well as that of goods. The Commission has not ruled out the possibility of a provision obliging all members to stop systematic checks at internal borders by the deadline. Agreement, however, seems close on some of the other obstacles to freeing borders, namely VAT harmonization, consistent laws on the restitution of illegally exported artistic goods and national treasures, and cross-border payments systems. National legislation of a substantial number of proposals still had to be enacted, however.

The White Paper marked an important shift in the EC's approach to integration. Whereas past efforts had focused on replacing existing national laws with uniform Community-wide measures, the Commission's approach to harmonization shifted with the Single European Act to the mutual recognition of national laws and regulations, subject to agreement on certain essential minimum requirements. For example, product standards, testing and certification requirements of each member state would be accepted in all member states provided they met a short list of minimum safety requirements prescribed by the EC. The proposed minimum corporation tax and VAT follow the same approach. This greatly simplifies the requirements for harmonization and places greater reliance on market forces as opposed to bureaucratic rules to ensure an eventual convergence of regulatory systems within the EC. In particular, market forces would create pressures on national governments with relatively restrictive rules to liberalize them so as to enable firms from that country to compete more effectively on an EC-wide basis.

Implementation of the single market program will affect the EC's trade relations with the rest of the world. For instance, the removal of internal borders implies that national trade restrictions against third countries will either need to be scrapped, or replaced by EC-wide measures that may be either less or more restrictive than existing national restrictions. Similarly, regulations governing the establishment and operation of non-EC firms in the EC may be either more or less restrictive than existing national regulations. The EC Commission has argued in favor of an open trade regime after 1992, and has stated that protection in the EC will not increase, on balance, as a result of the single market program. Indications thus far are that the post-single market external regime will broadly maintain--but in some cases may increase--the current degree of restrictiveness. There is already an agreement to replace national VERs with an EC-wide VER on Japanese car imports, and an EC-wide banana import regime is under discussion. Article 115, which allows individual members to request the Commission to ban certain imports circulating in other member

states, was renewed in December 1991 in the Maastricht Treaty. While recourse to Article 115 has declined in recent years, its continued existence is a potential source of protection, and runs counter to the spirit of the single market.

The EC has generally taken the view that the benefit of access to the unified market provides an opportunity to obtain reciprocal market-opening measures in trading partners. 1/ Reciprocity considerations have in fact become an integral part of the program, although the nature, scope, and means of implementation of reciprocity provisions are not yet fully defined. In areas such as services and direct investment, reciprocity provisions based on the principle of comparable market access (i.e., the same treatment for EC firms in foreign countries as firms from foreign countries enjoy in the EC) might succeed in opening up foreign markets, but could also be used as a tool of protection. Reciprocity provisions based on national treatment (i.e., the requirement that foreign firms receive treatment no less favorable than domestic firms) are less likely to act as a barrier to trade. Other forms of reciprocity affecting trade in goods have been proposed by some EC members. These include greater access to foreign country markets for EC producers in exchange for the removal of national restrictions in the EC. In some sectors, such as automobiles, attempts have been made by industry representatives in some EC countries to define greater access as the achievement of certain target foreign market shares for EC suppliers rather than as the reform of regulations or practices that have been identified as a barrier to market access abroad. In the EC's proposal for a tax on carbon emissions and energy to protect the environment, a defensive use of reciprocity is used: the proposal is made subject to the condition that trading partners adopt similar measures.

In the area of technical standards, reciprocity could take the form of mutual recognition treaties between the EC and third countries, under which single point access 2/ would be granted only to those countries that accept EC standards, testing, and certification procedures. The EC standards bodies invite public comment on their proposed standards with a view, inter alia, to providing transparency for EC standard-setting procedures. 3/ Industry representatives from non-EC countries have nevertheless expressed concern that standards and certification procedures may be used in a discriminatory manner to favor EC producers. GATT rules in this area are covered in the Tokyo Round Agreement on Technical Barriers to Trade (to which the EC is a signatory), but this stipulates only generally that technical regulations may not be used as a barrier to trade. Agreement in the Uruguay Round would make these rules more transparent.

1/ See, particularly, Hufbauer (1990), pp. 34-36.

2/ Under single point access, a product that meets technical standards in one EC member would have access to other EC members.

3/ EFTA countries already collaborate with the EC in drawing up standards under an agreement reached in 1988.

b. Implementation of White Paper

Implementation of the single market program has gained considerable momentum. The Commission succeeded in submitting all 282 proposals to the Council by April 7, 1990, and by mid-1992 over 90 percent of measures needed to implement the single market had been adopted. Transposition of directives into national legislatures has been slower. Some 75 percent of Directives had been transposed into national legislation by mid-1992 (with legislation in Belgium, Spain, Ireland, and Luxembourg being implemented more slowly), leaving open the possibility that many are unlikely to enter into force by January 1, 1993.

The single market program's efforts to eliminate intra-EC barriers to trade in goods focus on three main elements: simplification of cumbersome internal customs procedures, reduction of costly technical barriers to trade, and the further opening of government procurement. As regards customs procedures, the introduction of a single administrative document (SAD) on January 1, 1988, and the subsequent adoption of a directive eliminating the need for transit documents (for imported goods passing through one member state to another) as from January 1, 1993, are seen as important steps to facilitate intra-EC trade. The Council and Parliament have been discussing a customs code, which would provide a single reference for customs officials administering controls. Directives for veterinary and plant checks and for weapons controls are due to enter into force in 1992. To reduce the need for controls on national treasures, the Commission has made a proposal (in 1992) to harmonize members' laws on the return of illegally expropriated goods by countries in possession of valued national art and artifacts.

As noted above, the "new approach" to standards aims at reducing technical barriers to trade through the mutual recognition of national regulations among EC states, subject to certain minimum harmonizing criteria. 1/ These criteria are set out in "framework directives" which address such matters as safety, public health, and environmental protection.

1/ Even before the adoption of the Single European Act, differences in technical standards were not, in principle, supposed to impede the free movement of goods among EC countries. In its 1979 ruling in the case of "Cassis de Dijon," the European Court of Justice ruled that any good whose characteristics complied with regulations of the country where it was produced could be sold without restrictions in all other EC countries, regardless of their own standards, unless the restrictions were allowed under Article 36 of the Treaty of Rome. These exceptions would include restrictions for reasons of public morality, public policy, security, the protection of human, animal and plant life and health, and the protection of individual or commercial property. The Court identified four values that could theoretically justify anticompetitive restrictions: effectiveness of fiscal supervision, protection of public health, fairness in commercial transactions, and the defense of the consumer.

The first framework directive, concerning toy safety, was adopted in 1987 and entered into force on January 1, 1990. A product certified in one member state as meeting these requirements can be freely marketed in any EC country. Eight member states have passed implementing legislation. A second EC product safety directive, covering simple pressure vessels, due for implementation on July 1, 1990, has been postponed for two years, pending completion of a full set of reference EC standards. A third directive, on electromagnetic compatibility, came into force January 1, 1992, but standards for this area have not yet been developed. The directive contains a four year transition period during which national regulations will still apply.

Unlike customs procedures and technical standards, which are not necessarily intended to restrict trade, the purpose of "buy national" regulations in government procurement is to protect domestic suppliers. Certain sectors, such as utilities, often follow "buy national" policies. In June 1992, the Council of Internal Market Ministers reached an agreement in principle on a Commission proposal to open public procurement contracts to non-EC placement firms to four previously excluded utilities sectors: water, energy, transportation, and telecommunications. The Utilities Directive is expected to enter into force in most member states on January 1, 1993, with derogations for later implementation by Spain (January 1, 1996), and Greece and Portugal (January 1, 1998). In order to meet French, Spanish, and Italian fears that other EC member states may not adopt the same rules of fair competition in public procurement, the Directive allows for renegotiation and, ultimately, retaliation if a country closes its public procurement to EC firms. All legislation needed to open public procurement has now been proposed and most has been adopted. Once adopted, the legislation will open public contracts above certain threshold levels to competitive bidding in the areas of public supplies, public works and most public services. Compliance measures have been introduced for most areas, enabling suppliers and contractors to seek redress for unfair discrimination.

The Utilities Directive contains a "buy European" clause that would allow member states to reject bids from non-EC companies offering products with less than 50 percent EC content without additional justification. Moreover, even if the local content objective for services were met, member states would be allowed to apply a 3 percent preference to bids submitted by EC companies. The Directive would not interfere with the rights of foreign suppliers under existing or future international or bilateral agreements. The United States has expressed concern about the Directive's lack of predictability in its treatment of foreign products, and it has requested member states not to transform these guidelines into binding requirements. The United States is seeking to modify "buy national" policies in the renegotiation of the GATT Government Procurement Code. Similarly, the EC sees the Uruguay Round as an opportunity to negotiate with the United States over its "Buy American" program. In the context of these negotiations, the EC is seeking to ensure that the GATT Procurement Code will apply equally at

the level of national, regional and local entities, in the sectors of utilities and in procurement of services (including public works). It has expressed its willingness to commit itself to equivalent opening of its own procurement market in this context. In February 1992, the Council endorsed a directive to set up a monitoring service on public service contracts.

The modality for phasing out existing national restrictions on third country imports (or replacing them with EC-wide measures) has generated much debate. The debate is rooted in the large disparities across EC countries in the levels of protection and the competitiveness of the affected industries. Different national restrictions are inconsistent with the single market program and will be difficult to monitor once this is in place. An important example of national restrictions is the automobile sector. Imports of automobiles from Japan into the markets of France, Italy, Spain, Portugal, and the United Kingdom have been limited to varying degrees through VERs. ^{1/} In July 1991, there was agreement to convert national VERs on Japan's automobile exports to EC countries to an EC-wide monitoring arrangement (see Section III.3.a). Informal consultations between Japan and the EC have resulted in an apparent freeze on Japanese auto exports to the EC at 1.23 million units a year until 1999, replacing national restrictions, and to be monitored at the EC-level. Some of the EC countries now protected by VERs (France, Italy, and Spain) have argued that the automobile industry must remain an exception to the multilateral approach because of its economic importance and the large share of manufacturing jobs it provides within the Community. Moreover, some industry representatives have continued to argue that the phasing out of existing restrictions, even over the longer term, would need to be conditional on the achievement of specific target market shares for EC producers in Japan so as to bring bilateral trade in automobiles more closely into balance. Under current proposals in the Uruguay Round, the EC's VERs on autos from Japan would be excluded from the general requirement to phase out voluntary restraints within 4 years.

A major step toward the completion of a single European market for financial services was taken in December 1989 with the Council's adoption of

^{1/} The VERs maintained by Italy and Spain are government-to-government import quota arrangements which are approved by the Commission and are enforced through Article 115 authorizations limiting imports of Japanese autos transiting through other EC countries to Italy and Spain. The VERs maintained by France, Portugal, and the United Kingdom are industry-to-industry arrangements, some of which are quota-based, which are not recognized by the Commission and may not be enforced through Article 115 authorizations. These are enforced through national licensing and technical barriers to trade (including administrative guidance to importers, standards, testing and certification procedures, and the issuance of registrations by the national authorities).

the Second Banking Directive: 1/ The Directive, which will enter into force on January 1, 1993, will allow any EC-based credit institution to conduct the same kind of activities throughout the EC that it is authorized to conduct in its home member state, subject to a minimum capital requirement of ECU 5 million and certain other prudential requirements. 2/ The principle of mutual recognition underlying the Directive, which implies that banks from a second EC country could be authorized to conduct a wider range of activities than home country banks, is expected to create pressure for broad and uniform banking regulations across the member states.

The Directive stipulates that "the Community intends to keep its financial markets open to the rest of the world" with a view to promoting "the liberalization of global financial markets in third countries." Toward this end, member states will be asked to report any difficulties encountered by their credit institutions in establishing themselves or conducting business in third countries following the Directive's entry into force. Whenever it appears to the Commission that a third country has not granted effective market access to EC banks comparable to that granted by the EC to banks from that country, the EC may initiate negotiations aimed at securing comparable competitive opportunities. If, in addition, it appears to the Commission that the third country is not granting national treatment to the Community institution, the member state concerned may limit or suspend new requests for banking licenses from that third country. However, no limitations may be placed on the EC-wide operation of subsidiaries of third country banks already established in the EC. The same is not true for branches of foreign banks, which do not gain the new single banking license and the extensive freedom of establishment and operation associated with it. Rather, they essentially remain subject to the bilateral arrangements concluded between the branch's home country and the host member state.

The provision to negotiate effective market access was motivated by the concern that trade liberalization based simply on national treatment might not adequately compensate the EC for its trade concessions if domestic regulations in the EC were more liberal, in the sense of providing greater market access, than those of the EC's trading partners. Of particular concern to the EC are regulations in Japan and the United States which prevent credit institutions from engaging in both commercial banking and securities activities (the EC allows universal banking) as well as U.S. restrictions on inter-state banking. A reform of Japan's banking and securities business now allows banks and securities houses to handle a certain amount of each other's business through subsidiaries from January 1993. The United States has called on the EC to maintain a flexible approach to the question of effective market access in future framework

1/ The Second Council Directive on the Coordination of Laws, Regulations and Administrative Provisions Relating to the Taking Up and Pursuit of the Business of Credit Institutions.

2/ Other harmonizing provisions are set out in the companion Directive on Solvency Ratios, also adopted by the Council in December 1989.

directives, including those dealing with investment firms and insurance companies.

Continuing the process of opening up financial markets and harmonizing regulations for the single market, EC Finance Ministers have agreed (in June 1992) to proposals on an Investment Services Directive (ISD) and a Capital Adequacy Directive. These interdependent Directives establish minimum requirements for the authorization of securities firms and set regulation procedures, allow investment firms to operate freely in the EC, and establish minimum capital requirements for banks and firms trading in securities. The Directives, which have to be ratified by the EC Parliament before being finally approved by the Council, are seen as the last major element completing the unified market in financial services. Stockbrokers licensed in one member state will have the right to trade shares directly in any other EC member, and the common standards agreed for the disclosure of prices and volumes of transactions and for capital adequacy requirements should put all EC firms on an equal footing. EC subsidiaries of non-EC firms operating on the effective date of the ISD will be eligible for EC-wide authorization. Reciprocity considerations will guide treatment of applications from non-EC firms after that date. A timetable was also agreed for admitting banks to stock exchanges. Belgium, France and Italy are to grant banks direct access to their stock markets by the end of 1996, and Greece, Spain and Portugal by end-1999 at the earliest. EC Ministers have also agreed on liberalizing the non-life insurance sector. The third non-life Directive will enter into force in mid-1994 and allow insurance services to be provided throughout the Community on the basis of a single EC passport. Once a firm is authorized to trade in one member state, it can trade throughout the EC. Authorization is on the basis of a set of minimum standards, which can be expanded by individual members.

Trade in transportation services has traditionally been constrained by extensive national restrictions. Cabotage (the right to provide transportation services within any other member state) has generally been prohibited, while cross-border transportation has been subject to restrictive bilateral agreements. The Commission has established objectives for the transportation sector that include the right of establishment, the right to provide transportation services between any two member states, and cabotage. The Commission has also called for clarification and simplification of the role of the state in the transportation sector. Some progress has already been achieved in these areas. For example, limited cabotage in road transport went into effect on July 1, 1990, and EC Transport Ministers agreed on the deregulation of maritime cabotage in Europe in June 1992. Agreement was also reached by EC transport ministers in June 1992 on a "Third Aviation Package" under which EC airlines can, from January 1993, set their own fares on EC flights and operate between any two EC countries. Partial liberalization in 1993 will be followed by full liberalization of access and common air licensing and capital adequacy standards within the EC by April 1997. However, much work remains to be

done on road haulage, state aid to the transport sector, and Commission proposals for a second, more far-reaching phase of air transport liberalization covering prices on international fares (still to be set by governments), market access, capacity, and competition.

Telecommunications services have traditionally been provided by national monopolies in EC member states, with the role of private companies limited to providing equipment. Efforts have recently been made to open the sector to competition and to harmonize standards to allow interconnections. A Green Paper issued by the Commission in 1987 forms the basis for the current action program. The Commission, acting under its own authority, issued two Directives liberalizing the telecommunications equipment market. A third, harmonizing technical standards, was adopted by the Council of Ministers. In November 1991, a common position was reached on the Open Network Provision Directive which aims at harmonizing rules and standards for obtaining access to post, telephone and telegraph (PTT) networks. In January 1992, the Council adopted a resolution to harmonize technical standards for satellite communications. The EC's pursuit of competition policy--see Section V--also supports the liberalization of the telecommunications sector. Guidelines published in September 1991 apply Article 85 (on restrictive practices) and Article 86 (preventing the abuse of a monopoly position) to telecommunications. The Commission nevertheless cleared Alcatel's purchase of Telettra in 1991 even though it created high market shares in the transmission equipment market in Spain. As an important step in deregulating the sector, the EC Council agreed in principle, in mid-1992, to open up public procurement contracts in telecommunications to non-EC firms.

The Television Programming Directive was adopted by the Council in October 1989. Whereas earlier drafts of the controversial Directive had envisaged legally binding limits on the share of broadcast time devoted to foreign programs, the final version of the Directive took the form of a recommendation that the majority of air time should be reserved for programs of EC origin "where practicable" and "by appropriate means." The United States has held consultations with the EC under GATT on the Directive, which it considers to be inconsistent with the EC's GATT obligations and "the most disappointing single market directive adopted in 1989." ^{1/} For their part, EC officials have defended the Directive as a cultural measure. They maintain that television programming is a service and therefore reject U.S. claims that the Directive is inconsistent with existing GATT rules. In 1991, the United States Trade Representative placed the EC on the Special 301 "priority watch list" because of the Broadcast Directive, and is pursuing the matter in the Uruguay Round services negotiation.

The Directive on capital movements provided for the complete liberalization of capital movements in eight member states by July 1, 1990. Four Community members (Ireland, Greece, Spain and Portugal) are allowed by

^{1/} United States Government Task Force on the EC Internal Market (1990).

the directive to keep certain restrictions on the movement of short-term capital, temporarily until the end of 1992. Capital liberalization is also advancing in these four member States and in certain cases, notably in Spain and Ireland, progress in the liberalization process exceeds their respective obligations.

In the area of company law, the Council adopted the Regulation on Merger Control in December 1989, 16 years after the measure was first proposed. The regulation, which became effective in September 1990, requires companies planning a merger with a "Community dimension" to seek the Commission's prior approval. The regulation applies only to mergers that would result in a worldwide turnover in excess of ECU 5 billion, a higher threshold than the one proposed by the Commission. For a detailed discussion of the application of competition policy, see Section V.

The convergence of indirect taxation among member states remained an unresolved issue as the deadline for the single market approached. "The harmonization of legislation concerning turnover taxes, excise duties and other forms of indirect taxation" was provided for in the Single European Act 1/ "to the extent that such harmonization is necessary to ensure the establishment and the functioning of the internal market ...". The prospect of the removal of border controls led the Council in 1991 to adopt a new system--the postponed accounting system--to allow different VAT rates to exist until 1997. 2/ The Council also agreed in 1991 on a minimum standard VAT rate of 15 percent with some minimum reduced rates at 5 percent, and lower reduced rates for a transitional period. 3/ VAT rates diverge substantially in member states, from a standard rate of 25 percent in Denmark to 14 percent in Luxembourg and Spain. The issue is how far harmonized rates are necessary for the single market, with opponents pointing to different rates set in different states in the United States. Minimum excise rates on the main alcohol, tobacco, and petroleum products were also agreed in 1991, subject to review every two years, but these are still to be confirmed.

The Single Act of 1987 added to the Treaty of Rome the requirement that environmental protection should be part of all EC policies. The Maastricht Treaty (in Article 130r) went further and identified the objectives of provisions to protect the environment that could be adopted by the Council and included some broad parameters on financing. Under the fifth Environmental Action Program (for 1993-2000) proposed by the Commission in March 1992, the EC seeks stronger tools to ensure compliance with environmental directives and targets five sectors--agriculture, energy, industry, transport and tourism--for action. At present, the Commission can

1/ Article 99.

2/ See Kopits ed. (1992) for a detailed analysis of these proposals and their potential impact on trade.

3/ EC finance ministers agreed provisionally on the minimum VAT rate in July 1992 and on the retention of some zero rates.

take action against member states under Article 169, which allows the European Court to condemn breaches of environmental directives. An Environment Protection Agency is to be established.

A number of issues on the implementation of the environment program still remain to be resolved. On trade in waste, the major issue is whether each member should process its own waste, with trade only by specific agreement, or whether the Commission's proposal for regulating such trade should be accepted. The Commission has also proposed a draft Directive (in May 1992) to limit carbon emissions to 1990 levels by the year 2000 through energy conservation and a tax on CO₂ and energy. 1/ To meet strong opposition from EC industry, a conditionality clause was attached to the Directive making it subject to the adoption of similar measures by trading partners. Neither the United States nor Japan support such measures, while within the EC, Germany--which is unilaterally committed to reducing CO₂ emissions--has criticized the conditionality clause. Agreement on the Directive has stalled.

Progress is, however, being made in other areas. The Commission is proposing the introduction, on a voluntary basis, of an "eco-audit" for companies to carry an "eco-label" adopted by the Council of Ministers in December 1991. The audit would cover energy efficiency, waste production, site safety and overall impact on the environment. The Commission is to set Community-wide criteria which will be used by national entities established to assess the eligibility of products to carry the label. National entities are to be established during 1992.

Progress on freeing the movement of people within the EC has been limited. Participants in the Schengen Agreements--France, Germany, Belgium, Luxembourg, Italy, Spain, and Portugal (Greece is an observer)--accept the principle of allowing free movement of people, while the United Kingdom, Ireland, and Denmark are opposed. The Schengen countries have agreed to eliminate passport controls on internal air travel once the Convention comes into force, but checks will continue on flights between the group and EC countries that are not signatories. Issues of concern to nonparticipants in the Agreements are the employment of immigrants in other member states, drug trafficking and terrorism, and the ratification of the Dublin Convention on asylum policy.

The integration of the EC market has been accompanied by moves toward establishing a monetary union within the EC. 2/ This goal, initially

1/ See World Bank (1992(a)) and Hoeller and Wallin (1991) for a discussion of carbon taxes. Hoeller and Wallin find that a \$100 tax per ton of carbon added to current fuel prices in all countries could reduce carbon emissions in industrial countries by about 25 percent in the long run.

2/ This issue is discussed in detail in Ungerer et al., "European Monetary System, Developments and Perspectives," IMF Occasional Paper No. 73, 1990.

announced at the European Council summit in the Hague in 1969, was reasserted at the summit in Hanover in June 1988, when the Council appointed a committee (the Delors Committee) to propose concrete stages leading to economic and monetary union (EMU). The Delors Committee Report (1989) proposed a three-stage approach to EMU. The first two stages would involve the gradual elimination of all barriers to free capital mobility within the EC, participation of all members in the exchange rate mechanism of the European Monetary System (EMS), and greater coordination of monetary policies under the existing system of separately managed currencies. Full unification would be achieved in the third stage, in which a single currency would be adopted and monetary management would be transferred to the European System of Central Banks (ESCB). Implementation of the first stage began in June 1990 with the lifting of remaining exchange restrictions among EC countries; 1/ and the second stage is expected to occur in January 1994. Proponents of EMU argue that mobility of factors of production would be facilitated by reduction in transaction costs associated with exchange rate risk; increased mobility of factors of production would, in turn, facilitate adjustment in a single currency area. 2/

3. Interactions with Uruguay Round

The outcome of the Uruguay Round of multilateral trade negotiations will have an important impact on the EC's external regime after 1992. In particular, the negotiations on agriculture, services, market access, safeguards (including VERs) and textiles have a direct bearing on the EC regime that will emerge after national restrictions are lifted.

When this paper was written, complex issues in the Uruguay Round were still under discussion, especially in the key area of agriculture. Agreement in May 1992 on the reform of the CAP (see Appendix I) helped bring the EC position closer to some of the provisions on agriculture under the Draft Final Act (DFA), although other aspects remained to be resolved. (The DFA text on agriculture is discussed in more detail in Section III.3e.) In addition to the issue of the appropriate size of the reduction in the volume of subsidized exports, the EC was concerned, inter alia, that its new system of direct farmer support should not be subject to reduction, and that EC agricultural policies should not be subject to challenge in the GATT (the "peace" clause). Negotiations on other issues such as services and market access have not been finalized and are pending resolution of agriculture. The EC, as an important service exporter, should benefit significantly from a global liberalization in services. The DFA includes a consolidated text on services, and the Group of Negotiations on Services, which is to take negotiations forward, was still discussing the scheduling of bilateral concessions in June 1992. In particular, the EC has sought liberalization

1/ Postponed implementation is allowed for Greece, Ireland, Portugal and Spain, who are permitted to keep certain restrictions on the movement of short-term capital until the end of 1992.

2/ See Mundell (1961).

in maritime transport, financial services, and in the government procurement of telecommunications. On nonagricultural market access, the EC is seeking a lowering of tariffs across the board and reduction of tariff peaks in sectors of particular interest, such as textiles, shoes, ceramics, and glass.

The outcome of negotiations in other areas in the Uruguay Round will also affect EC policies. In particular, the agreement on safeguards will affect the role of VERs in the single market. The EC had argued for selective safeguards; the DFA takes this partly into account by allowing--within the general principle of uniform application of safeguards--for departures in specific circumstances. "Grey area" measures (such as VERs and orderly marketing arrangements) are prohibited, and existing ones must be phased out or brought into conformity with the agreement within four years of the agreement entering into force. The DFA allows for maintaining one such specific measure after the deadline; the EC has chosen the permissible exception to be VERs on cars imported from Japan. EC policies on dumping will be affected by the DFA which clarifies and tightens rules on dumping. The DFA text establishes criteria to identify circumvention through final assembly using products with minimal value-added subject to antidumping duties.

The EC (along with several other industrial countries) had resisted calls for a speedy liberalization of existing restrictions on trade in textiles and clothing. The DFA provides for gradual liberalization of trade in textiles and clothing, and its incorporation (backloaded) into the GATT framework, with all MFA restrictions to be eliminated by January 2003. All MFA product trade (excluding that integrated under GATT transitional measures), whether currently under GATT rules or not, is included until 2003 under transitional safeguard measures of the MFA, which are potentially more protectionist than the GATT safeguard clause and require selective quotas without compensation. Under the single market program, national quotas would be replaced by EC-wide quotas distributed among member states on the basis of MFA quotas.

The EC, along with other participants, has supported the creation of a Multilateral Trade Organization (MTO), provided for in the DFA to represent an umbrella organization for all agreements under the GATT and those being negotiated in the Uruguay Round. The MTO would also oversee surveillance over trade policies of its members and collaborate with other international organizations including the Fund and the Bank. In this regard, the EC has indicated the importance it attaches to fostering better international coordination among monetary, fiscal, and trade policies and to ensuring greater exchange rate stability. The MTO would also integrate and strengthen the dispute settlement process, allowing for faster decisions and more uniform and equitable procedures.

III. Trade Policy Developments

1. Policy setting and external environment

The reduction in internal trade barriers that accompanied the implementation of the common external tariff in the 1960s contributed to a rapid expansion in intra-EC trade. Intra-EC exports grew from 38 percent of total EC exports (12 percent of world exports) in 1960 to 50 percent of EC exports (20 percent of world exports) in 1970 (Tables 1 and 2). In the 1970s, however, the trade-creating impact of the customs union began to wane, and although the share of intra-EC exports in total EC exports increased marginally during the decade of 1970s, the share of intra-EC exports in world exports declined. During the 1980s, the terms of trade improvement resulting from the decline in oil and commodity prices contributed to an increase in intra-EC trade, both as a proportion of total EC trade and world trade. Trade with third countries declined somewhat, with offsetting trends in trade with various trading partners. There was a marked decline in imports--as a percent of EC imports--from developing countries, which are primarily commodity exporters, and a considerable increase in trade with Japan and the Asian newly industrialized economies (NIEs), with imports from the latter two outpacing exports to these countries.

These developments occurred against the background of the global recession in the early 1980s, which led to a sharp decline in the growth of world trade and an intensification in protectionist pressures in industrial countries. These pressures persisted even after economic growth began to recover in 1984. In part, this reflected the unsuccessful attempts of EC governments, among others, to use commercial policy to reduce the growing trade imbalances and other consequences of inappropriate macroeconomic policies. More fundamentally, however, the persistence of these pressures reflected resistance to the unprecedented pace of change in the structure of world production and trade. In particular, the continued rise in the share of Japan and NIEs in industrial countries' imports of manufactures resulted in substantial competitive pressures on import-competing industries of industrial countries. At the same time, the new markets created in the NIEs for industrial countries' exports were intensely competitive, leading some industrial-country exporters to demand increased assistance from their governments in such forms as subsidized loans and the tying of aid projects to trade. Labor market rigidities in industrial countries have also contributed to demands for protection.

As industrial countries had bound most of their industrial import tariffs at low levels through successive rounds of multilateral trade negotiations, the rise in protectionism in the 1980s was manifested in a proliferation of nontariff measures. While quantitative restrictions were sometimes employed, these were subject to GATT disciplines and therefore generally avoided. Rather, increasing use was made of VERs, which are more ambiguous under GATT law (they are commonly referred to as grey area

measures because their legality under the GATT has never been fully tested even though GATT Article XI prohibits the use of quantitative export restrictions). By enabling importers to "target" restrictions squarely on the most efficient global producers (unlike GATT-sanctioned safeguards which must be applied on a nondiscriminatory basis) and by eschewing price-based measures, VERs introduced major new inefficiencies in the pattern of world production and trade. Other inefficiencies arose from policies designed to insulate particular sectors from the effects of exchange rate changes, and from a sharp rise in agricultural export subsidies which contributed to growing agricultural surpluses and budgetary problems in the EC. The rise in competitive pressures also gave rise to a more aggressive use of antidumping measures by the EC since the mid-1980s, increasingly directed at developing countries. ^{1/} In the 1990s, protectionist pressures have been contained partly in response to ongoing negotiations in the Uruguay Round.

2. Instruments of trade policy

As in other major industrial countries, the EC's trade policy instruments include tariffs, tariff quotas, quotas, variable import levies, VERs, import licensing, safeguard actions, antidumping and countervailing duties, price undertakings, rules of origin, and legislation permitting retaliation against unfair trade practices abroad. The EC is a signatory to all of the Tokyo Round Codes and Agreements. These deal with import licensing, government procurement, technical barriers to trade, trade in civil aircraft, subsidies and countervailing measures, antidumping measures, customs valuation, beef products, and dairy products. The EC has established rules of origin that designate traded goods as originating in specific countries for purposes of (a) granting preferential tariff treatment; (b) applying antidumping duties; and (c) enforcing quantitative restrictions. Compared with many other industrial countries, the EC makes frequent use of antidumping investigations and quantitative trade restrictions, including VERs.

Import licensing procedures are applied at the Community level as well as by some individual members for import control purposes. At the Community level, licenses are required for imports of industrial or agricultural products that are subject to quantitative restrictions or monitoring. Separate regulations apply for imports of textiles, and, until recently, for imports of products originating in state-trading countries (the latter's regimes have now been considerably liberalized). Automatic licensing is granted to imports that are subject to surveillance. The Commission is authorized to require licenses for imports that cause or threaten to cause material injury to Community producers or when "critical circumstances" make immediate action necessary. Licensing requirements, necessary to implement safeguard measures taken under Article XIX of GATT, are subject to EC

^{1/} See Finger et al. (1982) for evidence on the earlier use of antidumping and countervailing measures as a tool of administered protection.

Council confirmation. National restrictions on imports of goods from third countries that are in free circulation within the Community are enforced through Article 115 of the EEC Treaty or, if the restrictions are not officially recognized by the EC, through national import licensing procedures.

Agricultural trade is governed by a separate regime under the EC's CAP (see Section III.3.e below).

3. Recent trends in trade policies

a. Voluntary export restraints

On the basis of unofficial information compiled by the GATT Secretariat, the EC (as an importer) accounted for 60 percent of all VER arrangements in the world (excluding arrangements under the MFA) in the period from September 1987 to March 1989 (Table 3 and Chart 2). ^{1/} The VERs maintained by the EC were fairly evenly divided between national and EC-wide arrangements (national VERs totalling 96 out of 173). Several of these arrangements have originated from antidumping duties that were discontinued when VERs were implemented.

The bulk of VERs imposed by the EC restrain trade in agricultural products, textiles and clothing products, electronics and autos and transport equipment. The EC accounted for between 41 percent and 89 percent of all VERs reported worldwide in these sectors as of March 1989. About one third of EC VERs were targeted at developing countries, of which Korea accounted for one third. Another third of the total--63--was targeted at Japan, and the remaining third was about equally divided between other industrial countries and Central and Eastern European countries. The share of textiles, clothing, and footwear in total EC VERs tended to rise after September 1987, with a corresponding increase in the share targeted at developing countries.

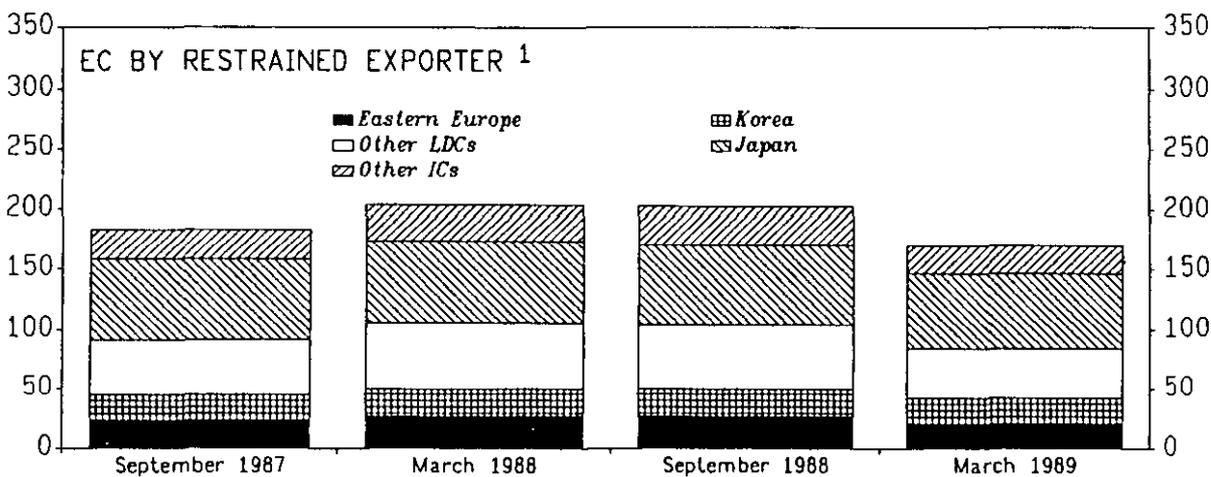
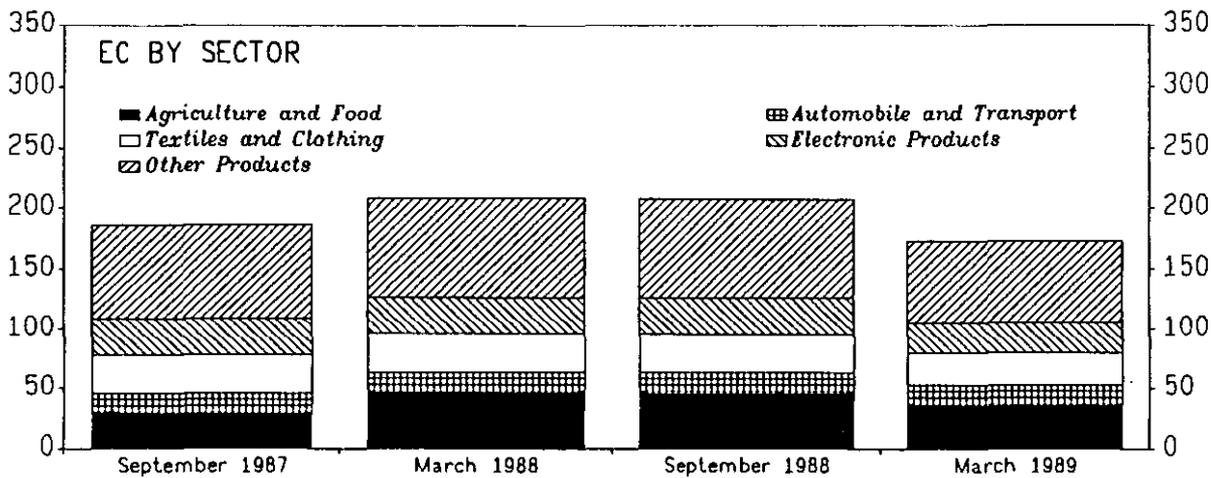
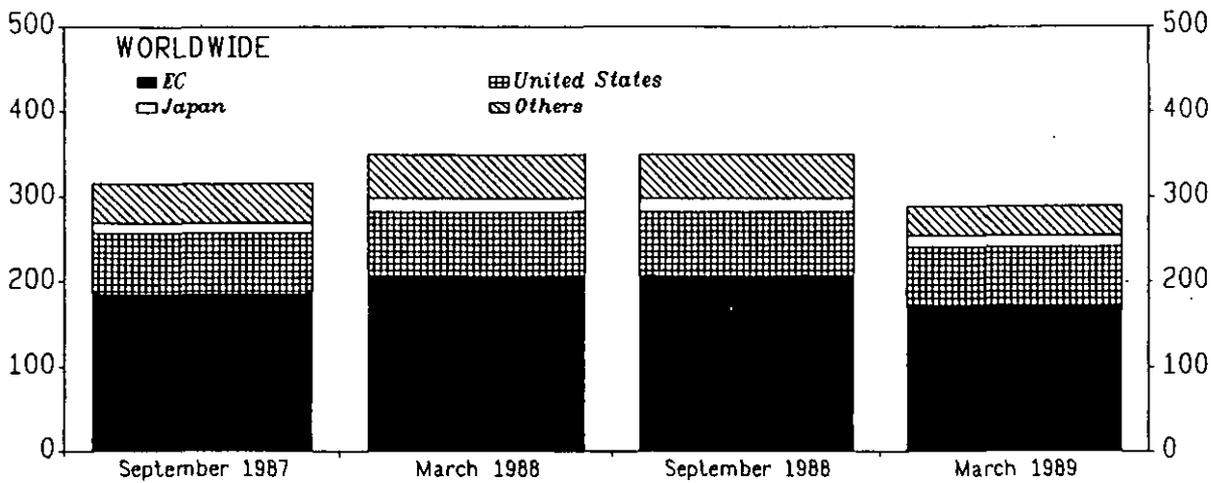
More recent information from the GATT ^{2/} on narrowly defined voluntary restraint measures shows the main product areas are still, in order of importance, agriculture, textiles, steel, electronics, and motor vehicles. Some export restraint arrangements with Japan in machinery, electronics and motor vehicles are accompanied by retrospective surveillance. This was stated to be necessary because the imports had been made at "relatively low prices, thereby depressing the price levels and financial results of the community industry and thereby threatening to cause injury." ^{3/} In January 1991, the EC decided to continue surveillance of certain Japanese goods, in particular the VERs on automobiles. As mentioned

^{1/} The GATT Secretariat has not compiled comprehensive data on VERs since March 1989.

^{2/} GATT (1991).

^{3/} Commission Regulation No. 653/83.

CHART 2
EUROPEAN COMMUNITY:
NUMBER OF VOLUNTARY EXPORT RESTRAINTS



Source: See source for Table 3.

¹ Unidentified countries excluded.

earlier (Section II 2.), national VERs on Japan's automobile exports to EC member states were converted in 1991 to an EC-wide monitoring arrangement.

b. Article 115 authorizations

Article 115 of the Treaty of Rome empowers the Commission to authorize a member country to apply protective measures against imports from third countries if such imports threaten the domestic production of the product concerned and cause injury. An Article 115 authorization temporarily restricts free circulation of goods within the Community and prevents circumvention of the national restriction through imports via other member countries.

Total authorizations under Article 115 gradually declined to 79 in 1990, and to 48 in 1991--just over one fifth of their 1980 level, and the percentage granted to the total requested has fallen (Table 4). The decline partly reflects a tightening of the criteria used by the Commission in assessing member countries' requests. This assessment is based on the evolution of the member country's imports of the item concerned relative to total EC imports as well as the industry's profit position and employment trends. By product, textiles and clothing continued to account for the bulk of Article 115 authorizations. However, their share in total authorizations declined from 74 percent in 1980 to 67 percent in 1991, with a corresponding increase in the share of other products, including electronics, machine tools, and footwear. By country, Spain accounted for about 42 percent of the total authorizations granted in 1991, followed by Italy and France.

The revision of the EEC Treaties at the Maastricht Summit in December 1991 maintained Article 115. Although expected to be invoked only rarely when the single market program is established in 1993, the continuation of Article 115 is a potential source of distortions.

c. Antidumping

The EC has made extensive use of antidumping instruments (Table 5), although usage had declined by 1991. In 1986, the last year for which comprehensive cumulative data are available, the EC maintained 123 outstanding antidumping actions, with the number of antidumping investigations initiated ranging from a low of 24 in 1986 (which the Commission attributed partly to its own staffing problems), to a maximum of 49 cases in 1984. In 1988, the last year for which comprehensive annual data are available on a comparable basis, 1/ 40 cases were initiated, about the same as in 1987. 2/ However, provisional antidumping duties were imposed in 28 cases in 1988, more than twice as many as in 1987, while the application of definitive antidumping duties doubled to 18. In 1990,

1/ Data through 1988 are available from the EC Commission (1990b).

2/ These data exclude investigations under the EC's "screwdriver" legislation, which are reported separately in Table 6.

the EC reported having initiated 43 new investigations, but less than half that number--20--in 1991. This decline continued to be accompanied by high levels of provisional and definitive duties; 19 cases of each in 1991 compared with 23 and 18, respectively, in 1990.

The share of antidumping investigations concerning imports from developing countries increased from about one quarter of the total during 1983-85 to about one half during 1986-88. Investigations involving developing countries have covered a wide range of products, including a variety of consumer electronics (e.g., small screen color televisions, telephones, cellular mobile radios), metals and minerals, food additives, textile products, video and audio cassette tapes, and some steel products. The People's Republic of China, Hong Kong, and Korea have been among the most frequently investigated developing country exporters, with other investigations involving Argentina, Brazil, Egypt, Indonesia, Macao, Taiwan Province of China, Thailand, Trinidad and Tobago, Turkey, and Venezuela.

Investigations initiated against industrial countries were targeted mainly at Japan and countries belonging to EFTA, and concerned a variety of products including consumer electronics, diesel engines, chemicals, and steel products. Investigations involving Central and Eastern European countries principally concerned chemicals and steel products.

The EC introduced new legislation in June 1987 that permits, in certain circumstances, the imposition of antidumping duties on products assembled in the EC by subsidiaries or affiliates of foreign companies. The legislation was intended to counteract perceived efforts by foreign companies to circumvent antidumping duties on certain imported products by setting up or expanding final assembly operations (referred to as "screwdriver plants") in the EC. 1/ Eight antidumping investigations were initiated in 1988 and 1989 under the new legislation, all of which were directed against Japanese companies that assembled products in the EC (Table 6). 2/ Of these, four resulted in the imposition of definitive antidumping duties, all of which were subsequently revoked on the basis of minimum price undertakings by the companies concerned. In May 1990, the GATT Council adopted a finding that

1/ Article 13(10) of the Council Regulation (EEC) No. 2324/88 provides that duties may be imposed on products if the following conditions are met: (i) the firm producing or assembling the product in the EC is associated with a foreign manufacturer whose exports of a like product is already subject to a definitive antidumping duty in the EC; (ii) the EC-based assembly or production operation was started or substantially expanded after the opening of the antidumping investigation; and (iii) the value of parts or materials originating in the country whose exports of the like final product are subject to the antidumping duty exceeds 60 percent of the final product.

2/ The eight products concerned are electronic typewriters, electronic scales, plain paper photocopiers, ball bearings, dot matrix printers, hydraulic excavators, earth-moving equipment, and videotape recorders.

antidumping duties assessed under the screwdriver legislation violated GATT rules on national treatment (Section V).

In 1986 the EC extended the concept of dumping to a service industry (shipping), which is not subject to GATT rules. An investigation was initiated against a Korean shipping company based on a complaint by EC shipping companies that it was practicing "predatory pricing" on the EC-Australia route. Despite objections to the shippers' complaint by EC exporters, who argued that the Korean fares permitted them to be competitive in the Australian market, definitive antidumping duties of 37 percent were imposed in January 1989, forcing the Korean shipping company to give up the EC-Australia route.

d. Rules of origin

The increase in Japan's direct investment in the EC in recent years and its perceived impact on the ability of EC firms to compete in their own market has raised the issue of defining origin rules for purposes of providing EC treatment to goods that are assembled in the Community. The issue of nationality of goods assembled in the EC or third countries using imported components arose in connection with the imposition of antidumping duties on such goods under the new EC "screwdriver" legislation, as well as in connection with the possible inclusion of such goods in VERs maintained by individual EC countries. In particular, the rising exports to other EC countries of automobiles manufactured in the United Kingdom by a Japanese company (Nissan) raised the issue of whether existing instruments of selective protection, such as national VERs and Article 115 authorizations, could legitimately be used to curb such exports. Current GATT rules (Article IX) extend certain disciplines, such as MFN treatment, to the use of marks of origin but do not define rules of origin per se. However, one of the proposals submitted to an early GATT working party was later adopted in the Kyoto Customs Convention of 1965. It states that: "The nationality of goods resulting from materials and labor of two or more countries shall be that of the country in which such goods have last undergone substantial transformation," (emphasis added). ^{1/}

Although the EC incorporated the Kyoto Convention definition in its 1968 origin regulation, it also gave the Commission authority to issue product-specific implementing rules "for controversial or new products." ^{2/} The Commission issued two controversial regulations clarifying origin rules for photocopiers (which are subject to antidumping

^{1/} This was the definition proposed by the French delegation to the 1953 GATT working party. See Jackson (1969) p. 468. The EC and the United States, but not Japan, have adopted the Kyoto Convention origin definition.

^{2/} Council Regulation 802/68, Article 5, EC Official Journal L148, 6/27/68. Since 1968, technical regulations have been issued for color televisions, radios, tape recorders, and meat and, in 1989, photocopiers and semiconductors.

duties when imported from Japan) and semiconductors. 1/ The regulation on photocopiers did not specify a local content rule but instead takes a negative approach by listing manufacturing operations that do not confer origin, including the last assembly operation. The regulation has been viewed as being tailored to deal with photocopiers manufactured by a Japanese company (Ricoh) in the United States. Under the regulation, these photocopiers are considered of Japanese origin and could be subjected to antidumping duties in the EC. The regulation on semiconductors similarly defined the last assembly operation as not conferring origin. 2/ This definition implied that EC producers of semiconductors could carry out the last assembly operation in low-wage third countries and still qualify for EC treatment, whereas third country producers who carry out only the last assembly operation in the EC would lose EC origin designation. Both regulations seem to indicate that the EC is moving toward a definition of origin based on the "most substantial" (and technologically most advanced) rather than "last substantial" transformation. Japan has expressed concern that EC origin rules may be used in a discriminatory manner against specific countries and products, and has submitted proposals for multilaterally endorsed origin rules in the Uruguay Round (Section IV.1).

e. Agricultural policies

The CAP provides the main framework for agricultural support in the European Community, although national support also remains important. 3/ Support mechanisms under the CAP cover about 85 percent of EC agricultural production. For most agricultural products, support takes the form of "target" prices that are the upper end of the range within which prices are permitted to fluctuate. At the lower end of this range is the "intervention" price at which specialized public entities stand ready to buy what is offered to them, albeit with reductions in recent years in both the volume and the time span of purchases of certain products. Intervention prices exceed world prices by considerable margins in most cases. Protection against imports is provided through variable levies set at a level that equalizes import prices to a reference price (often referred to as "threshold" price) set at around the middle of the range between target and intervention prices. For exports, variable subsidies--referred to as

1/ Commission regulations 2071-89, EC Official Journal (OJ) L196/24, 7/12/89 (photocopiers) and 288/89, OJ L33/23, 2/4/89 (semiconductors). Regulations issued by the Commission do not require Council approval and constitute Community law unless objected to by a member state within three months.

2/ The regulation specifies that the "diffusion operation," by which integrated circuits are transformed into semiconductors, confers origin. The diffusion operation is defined as the "last substantial operation" on the grounds that it is highly sophisticated technically and presupposes a large research investment.

3/ See Rosenblatt et al. (1988), for a detailed discussion of the CAP before the latest round of reform proposals.

export refunds--are provided to exporters to offset the difference between EC and world market prices. Some products with tariffs bound at zero in GATT are protected through VERs and supported by production subsidies. Quantitative import restrictions and the variability of import levies and export subsidies insulate the EC farm sector from exchange rate movements between EC currencies and those of competing suppliers. Exchange rate movements among EC currencies--other than within the narrow band of the EMS exchange rate mechanism--are similarly offset through monetary compensatory amounts (MCAs), to ensure the equality of agricultural prices expressed in ECUs within the Community.

Until 1988, financial support under the CAP was virtually open-ended. With no limits on what could be sold to intervention agencies at guaranteed prices, expenditures under the CAP more than doubled, from ECU 11.3 billion in 1980 to ECU 23.2 billion in 1987, reflecting the combined influences of expanding EC production and declining world market prices (Table 7). Under the pressure of these mounting budgetary costs, changes in the CAP's structure were introduced in February 1988. These included the introduction of restraints on intervention prices (effectively a freeze on nominal prices expressed in ECUs) 1/; guidelines limiting the overall level of EC agricultural support to 1.2 percent of GNP of the EC, and limiting the growth in agricultural support to no more than 74 percent of the increase in GNP of the EC; automatic stabilizers to reduce benefits when production exceeded quota levels; a shortening of the period during which intervention purchases could be made; and a land set-aside program. Price restraints involved a freeze in intervention prices (Table 8), but this was not effective in restraining production because of the high initial level of prices and productivity increases that compensated for price reductions in real terms. Also, the impact of price restraints were partly offset by the operation of MCAs, which permitted an increase in prices expressed in national currencies in 1987/88 (Table 9). Moreover, the 1988 reforms left import barriers intact and did not provide a mechanism to contain the growth in export subsidies. Budget expenditures reached a new peak of ECU 27.7 million in 1988.

Implementation of the CAP reforms in 1988 was followed by a marked deceleration in EC agricultural support payments which remained below their 1988 level in 1989 and 1990 (Table 7). The rate of assistance as measured by producer subsidy equivalents (PSEs) 2/ fell from a peak of 50 percent in 1986 to 41 percent in 1989 (Table 10). The improvement evident in the lower subsidies in 1989 was partially attributable to the introduction of production quotas (most significantly in the dairy sector), but much of the improved financial performance in 1989 can be traced to the increase in

1/ In terms of national currencies, and including adjustments in monetary compensation amounts, the average intervention price increased by 1.2 percent in 1989/90 and by 1.6 percent in 1990/91.

2/ The PSE is the equivalent subsidy that would be needed to provide producers with the same income if all support policies were removed.

world commodity prices (denominated in ECUs) in 1988-89 which significantly moderated the cost of export subsidies. As international commodity prices began to weaken once again in 1990, doubts resurfaced about whether the present structure of the CAP was sufficient to bring about a sustained reduction in financial support for agriculture. One immediate problem, with repercussions for the 1990 budget outturn, was that a fall in the Community's market price for beef was triggering large intervention purchases to stabilize the market. Another development, which had its full impact only in 1991, was a sharp decline in the world market price of wheat which threatened to drive up outlays on export subsidies. More generally, developments suggested that the financial impact of the automatic stabilizers and land set-aside program could have been smaller than initially expected. Thus, although agricultural expenditures in the draft budget for 1991 (ECU 30.4 billion) remained well within the guideline ceiling (ECU 32.5 billion) set by the 1988 reform, the margin was far smaller than in 1989-90.

By 1991, as commodity prices continued to weaken and production--particularly of cereals--strengthened, structural problems reemerged. Agricultural support payments rose by over 20 percent in 1991 after a small increase in 1990, to ECU 32.4 billion (Table 7). In 1991, subsidies were 49 percent of producer prices in the EC, compared with 30 percent in the United States and 66 percent in Japan (Table 10). Assistance per farmer measured by producer (Table 10) and consumer subsidy equivalents also rose. The OECD ^{1/} notes a 25 percent increase in total PSE payments in 1990, two-thirds of which was due to a higher unit PSE, and a 0.5 percent decline in 1991 from lower unit PSEs. The costs of the CAP also fall as an implicit tax on consumers. The OECD reports a consumer subsidy equivalent (CSE) to EC agriculture totalling \$63 billion in 1991, compared with \$84 billion in direct assistance to producers, and \$45 billion and \$60 billion of CSE and PSE, respectively, in 1989. The increase in 1991 was due to higher transfers (rather than volumes consumed) from lower United States dollar prices, partly offset by the depreciation of the ECU against the dollar.

Reflecting partly the higher costs of these subsidies, and partly a concern with growing surpluses (particularly of cereals, dairy products and beef), wide-ranging proposals for reform of the CAP were presented by the Commission in October 1991 (the MacSharry proposals). These were based on a perceived need to change the direct link between agricultural production and support and the incentives for higher production and intensification which created difficulties for market stability, farm incomes, the budget and the environment. The essential features agreed at a political level by the EC Ministers of Agriculture in May 1992 are given in Appendix I. This political agreement covered some 75 percent of marketed agricultural output and would be phased in over four years. Substantial reductions were envisaged in support prices, with offsetting payments to farmers. Target prices for cereals would be reduced from their present level of about

^{1/} OECD (1992).

ECU 155 per ton to ECU 110 per ton by 1995/96--a cut of 29 percent (the cut amounts to 35 percent comparing actual cereals prices with the target). Farmers would be compensated for this loss by income support--based on area under the crop in a base year and regional average yields. Large farmers would receive income compensation if they joined the scheme to set 15 percent of land aside--i.e., out of production--on a rotational basis. Set asides were not required for small farmers. Compensation rates are still to be determined. Intervention prices for beef were to be cut in equal steps by 15 percent by 1995/96, and prices of butter by 5 percent. Milk quotas remained for 1992/93 but beef and sheepmeat would be subject to new quotas. Other proposals covered the introduction of quotas for tobacco production. The CAP reforms were complemented by rural development measures to encourage environmental protection, afforestation, and restructuring by providing incentives for early retirement for farmers.

The recent CAP reform is a positive step in the evolution of the EC's trade and trade-related policies. It represents an important move toward reducing agricultural distortions over the next three years, although the reform process will need to be strengthened and sustained over a longer term if distortions are to be completely eliminated. The positive features of the current reform are the moves to bring domestic agriculture support prices closer toward world levels, to shift from reliance on subsidies through price supports toward direct income support, and to induce a reduction in the area under subsidized food production. Given that direct income support is replacing price support, the impact on the EC's budget may not be significant, at least in the next three years.

The agricultural text of the 1991 DFA under the Uruguay Round requires specific reductions in: export subsidies (a reduction of 36 percent in value and 24 percent in volume, between 1993 and 1999, from a 1986-90 base); domestic support measures (a 20 percent reduction in nominal support measures affecting prices and production decisions, between 1993 and 1999, from a 1986-88 base with credit for reductions since 1986); and levels of tariff barriers to market access (a simple average reduction of 36 percent, with a 15 percent minimum reduction on all tariff lines, from 1993 to 1999). The DFA also provides for the "tariffication" of all quantitative import barriers, but introduces a safeguard mechanism that would adjust for changes in world product prices and exchange rates up to a specified level. The agriculture agreement would be reviewed, and negotiations re-engaged, in 1998 (one year before the expiry of the proposed "implementation period").

The DFA classifies domestic support for agriculture into two categories: exempt or subject to reduction. To be exempt, domestic support should have minimal or no trade distorting effects and no effects on production--i.e., support should be delinked from production and prices. "Trade distorting" effects are defined to include government contributions in the form of public transfers, foregone revenue and income or price supports that confer a benefit. To be actionable, subsidies need to be production-related. Even if these subsidies meet the reduction requirements

proposed under the DFA, they may still be subject to dispute if they have adverse effects on other participants. In this situation, the burden of proof for serious prejudice would rest with the injured party.

Given the envisaged reduction in agricultural support prices over the next three years under the latest CAP reform, the reduction targeted in production subsidies over the next six years under the DFA is achievable. The adequacy of the CAP reform measures in meeting the DFA target on export subsidies (mainly in the area of exportable quantities) is less certain, and hence negotiations on this aspect were continuing at the time of writing. The question remains as to whether the new system of direct income support would be subject to reduction under the DFA or compromises would be reached. The EC is interested in a possible "rebalancing" (i.e., the ability to raise restrictions in one area in exchange for reductions in other areas), though this concept is not included in the DFA as currently drafted. The EC is also seeking assurances by trading partners that its agricultural policies will not be subject to challenge in the GATT.

4. Trade agreements

The EC maintains some 24 different preferential trading regimes covering more than 150 countries. These fall under two broad categories: reciprocal trade preferences negotiated with a number of countries or country groupings under association, cooperation or free trade agreements, and preferences granted on a nonreciprocal basis to developing countries under the EC's Generalized System of Preferences Scheme (GSP), and to 69 African, Caribbean, and Pacific countries under the Lomé Convention. Goods originating in the countries covered by these special regimes are, in principle, subject to zero or reduced tariff rates, provided they meet the origin rules specified in each agreement.

a. European Free Trade Association (EFTA) and the EC ^{1/}

Free trade agreements were concluded in 1972-73 between the EC and each of the six members of EFTA (Austria, Iceland, Norway, Portugal, Sweden, and Switzerland). ^{2/} These agreements provided for the phased elimination of tariffs and quantitative restrictions on industrial and processed--but not unprocessed--agricultural products. ^{3/} Trade between the two country groupings expanded rapidly in the years following the signing of the agreements, but in the early 1980s, the growth in trade slowed and even reversed. By 1984, it was recognized that the scope for furthering trade in the context of the existing agreement was limited, and EFTA countries became

^{1/} A comprehensive discussion of EC-EFTA economic relations is contained in Abrams et al. (1990).

^{2/} Finland was an associate member of EFTA until 1986, when it became a full member.

^{3/} Agricultural trade policies in EFTA countries are, on the whole, more restrictive than those in the EC.

concerned that the EC initiatives toward internal integration could reduce access for EFTA countries to the EC market. These factors contributed to EFTA's decision to seek closer links with the EC, and for EFTA members to consider joining the EC. A ministerial meeting between EFTA and the EC in November 1984 resulted in the announcement of a program for cooperation contained in the Luxembourg Declaration. The Declaration included commitments to reduce technical barriers to trade, eliminate quantitative export restrictions, revise rules of origin, and open up government procurement. Subsequent ministerial meetings expanded the scope of EC/EFTA cooperation to increase the transparency of state aids and simplify border formalities.

Despite these renewed efforts, further progress in removing trade barriers between the EC and EFTA was slowed by the fact that EFTA, in contrast to the EC, lacked common rules in the areas under negotiation, e.g., on the provision of state aids. In addition, as a more informal group, it had limited capabilities for coordinated decision-making and action. Against this background, the heads of government of the EFTA countries in March 1989 issued a declaration setting out the goal of creating a more structured partnership with the EC by strengthening their internal decision-making process and fostering EC/EFTA institutional links.

The idea of creating a European Economic Space (EES) with a minimum of impediments to trade, was approved in principle by EC and EFTA foreign ministers in December 1989, and formal negotiations were launched in June 1990. ^{1/} In principle, the EES would expand the EC's single market to the other seven European economies, which would, in turn, adopt most of the legislation and disciplines of the single market. The negotiations were accordingly to focus on two issues: (i) the extent to which the non-EC countries will henceforth have input in the formulation of EC single market policies; and (ii) the degree to which the non-EC countries will be granted exceptions under the EES to EC single market rules and disciplines (e.g., in the areas of state aids and agriculture).

In October 1991, agreement was reached at an EC-EFTA Ministerial meeting on the terms of a European Economic Area--EEA (as the EES came to be called) to be established on January 1, 1993--the same date that the single market comes into being. It provides for the free movement of goods, persons, services and capital, creating a unified market of 19 countries. There are also provisions on competition and state aid, as well as (among others), social and environmental policy, consumer protection and education. As for derogations, the EFTA countries obtained limited transition periods in a number of areas but virtually no permanent exceptions. The EEA does not cover agriculture in general but there are limited provisions aimed at improving market access for processed agricultural goods. The EFTA

^{1/} Liechtenstein has been a member of EFTA since early 1992 and is also participating in the negotiations on the EEA along with the other six EFTA members. See Winters (1992) for a discussion of the impact of the EEA.

countries have little authority to influence policymaking and legislative developments in the EC--and by extension in the EEA--a result that has most probably contributed to their interest in full EC membership. (Four EFTA countries--Austria (1989), Sweden (1991) and Finland and Switzerland (1992)--have already applied for EC membership and Norway is actively considering membership). The EEA agreement does not provide for participation by EFTA countries in the debate on the monetary and political unions. EFTA countries will affect future EC laws influencing the EEA through the institutions (the EEA Council and the Joint Committee) established to set EEA policy. The treaty was approved by the EC Court in April 1992, and signed by the EC and the EFTA in May. It now needs to be ratified by national parliaments and the European Parliament by the scheduled date of January 1, 1993 to coincide with the completion of the EC internal market. The agreement provides for an EFTA monitoring authority and an EFTA Court to settle conflicts between EFTA members. The EC and the EFTA monitoring authorities will handle complaints under their jurisdiction and transmit complaints falling under the authority of the other body.

b. Association and Cooperation Agreements

The EC has signed Association Agreements with Cyprus (1972), Malta (1970), and Turkey (1963) providing for reciprocal tariff preferences, aid, industrial cooperation, technical assistance and, in principle, full accession to the EC after a transition period. 1/ The Czech and Slovak Federal Republic, Hungary and Poland signed Association Agreements with the EC in 1991 (see section c below).

In October 1987 Cyprus signed a protocol providing for a phased reduction of its tariffs on EC industrial exports and adoption of the EC common external tariff over a 10-year period starting in January 1988. 2/ The protocol also calls for reciprocal concessions on agricultural exports, and full liberalization of agricultural trade beyond the 10-year transition period. It is envisaged that within four to five years after the 10-year transition period, Cyprus would become a full EC member. In June 1990, Malta announced its intention to apply formally for full EC membership in the near future.

Turkey applied for membership in April 1987 but in December 1989 the Commission effectively ruled out EC membership for Turkey over the medium term. Nevertheless, the two parties are continuing to work toward their longstanding objective of completing a customs union by the end of 1995. Toward this end, Turkey began implementing unilateral tariff reductions in

1/ Greece, Portugal, and Spain had concluded association agreements prior to their full accession to the EC.

2/ Industrial exports from Cyprus to the EC have benefitted from duty-free access to the Community since 1977, with the exception of petroleum products, and certain textiles and clothing items that are subject to quotas.

early 1988. 1/ From January 1992, Turkey reduced duties by a further 10 percent on goods imported from the EC, and has reduced a number of customs duties. (Turkey signed a free trade agreement with EFTA countries in December 1991).

Trade and cooperation agreements were signed with Yugoslavia in 1973 and with Algeria, Egypt, Israel, Jordan, Lebanon, Morocco, Syria, and Tunisia in 1976-77. Under these agreements the European Community grants duty-free access to its markets for industrial exports of these countries and tariff concessions for certain of their agricultural exports, in addition to providing various types of aid and technical assistance. Exceptions apply to textiles and other "sensitive" products, and for agricultural products covered by the CAP. In most cases, benefits accrue to the EC through nonpreferential, MFN treatment of its exports to these countries and through better market knowledge. However, the agreement with Israel, which was concluded on the basis of Article 113 of the EEC Treaty, provides for an industrial free trade area. In line with the agreement, the EC removed all tariffs and quantitative restrictions on Israel's industrial exports by 1977. Israel, which was initially expected to dismantle its tariffs on industrial exports from the EC by 1985, was granted extensions until January 1, 1989, when the process was completed.

In an effort to compensate partially for the increased competitive challenges posed by the internal market program and by closer EC relations with Eastern European countries, in December 1990 the Council agreed to a budget for its programs with 12 Mediterranean countries during 1992-96 that represented a three-fold increase compared with the 1986-91 period. 2/

A cooperation agreement with the members of the Cooperation Council for Arab States of the Gulf (GCC) 3/ was signed in June 1985, providing, inter alia, for a standstill on trade restrictions and the mutual application of MFN treatment. 4/ In December 1989 the EC Council approved directives authorizing the Commission to enter into negotiations with the GCC with the view to reaching a free trade agreement after a transitional period. The implementation of the arrangement has been delayed by the single market program as well as slow economic integration within the GCC. At the most recent Ministerial meeting in May 1992, environmental issues were paramount, especially the EC proposal for an energy tax (see Section II.2.b). The GCC

1/ Under its association agreement, Turkey already benefits from duty-free access to the EC market for industrial and certain agricultural exports. Quantitative restrictions apply on exports of textiles to the EC, which take the form of an industry-to-industry VER, given that direct government involvement would contravene the association agreement.

2/ European Report (May 24, 1990), p.V.7.

3/ The members of the GCC are Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates.

4/ MFN treatment previously only applied to Kuwait, the only GCC country that is a GATT contracting party.

concerns focused on the adverse impact of an oil tax on domestic economic development and trade relations with the EC. The EC view was that the proposed combined carbon-energy tax would not affect the relative competitive position on oil. The EC is the main market for petrochemical goods from the GCC and is the largest supplier of the GCC's merchandise imports.

c. Relations with the former Council on Mutual Economic Assistance (CMEA) and East European Countries

Relations with former CMEA member countries 1/ have evolved rapidly following the signing of a joint EC-CMEA declaration of mutual recognition in June 1988. Bilateral trade and cooperation agreements were subsequently concluded with Hungary (September 1988) and Poland (September 1989) providing for the mutual granting of MFN tariff status and the phased elimination of discriminatory (country-specific) import restrictions by the EC. Similar trade and cooperation agreements were concluded with Bulgaria and Czechoslovakia in May 1990 and with Romania in October 1990. In addition, the EC extended certain GSP benefits to Hungary, Poland, and Czechoslovakia, which, for their part, undertook to promote a favorable investment climate for EC firms. In the event, the timetables for phasing out quantitative restrictions (originally scheduled for completion in 1994) were greatly accelerated, with the EC lifting all country-specific import restrictions vis-à-vis Hungary and Poland on January 1, 1990. GSP status was removed from these countries once the interim Association Agreements entered into force in March 1992.

Association Agreements (or Europe Agreements) were signed between the EC, Hungary, Poland and the Czech and Slovak Federal Republic in December 1991, after a year of negotiations, to establish a free trade area within, at maximum, ten years. These Agreements were submitted to national Parliaments and the European Parliament for ratification. 2/ Meanwhile, the trade provisions of the agreements entered into force as interim agreements on March 1, 1992. The agreements recognize that full membership is the final objective. They aim, in the interim, to provide a framework for political dialogue, to promote trade and economic relations, to provide a basis for financial and technical assistance, and lead to the countries' gradual integration into the Community. The agreements, which have a common framework, provide for preferential treatment and progressive reduction or abolition of tariffs on industrial goods (with exceptions, such as textiles, and coal and steel products). When the Agreements become effective, about 60 percent of imports into the EC will enter duty free and all quantitative restrictions except for those on textiles and coal and steel products from certain regions will be abolished. (The elimination of quantitative

1/ The members of the CMEA were Bulgaria, Cuba, Czechoslovakia, Hungary, Mongolia, Poland, Romania, the U.S.S.R., and Viet Nam.

2/ The Association Agreements with Poland and Hungary were ratified by the European Parliament in September 1992.

barriers on textiles and clothing will be linked to liberalization in the Uruguay Round, while restrictions on coal and steel products, which are covered in separate protocols, will be phased out over four years.) Liberalization will be asymmetrical, with EC concessions introduced faster than those in the Eastern European countries. Sensitive agricultural goods (including processed and fishery products) were excluded from the liberalization, although reciprocal concessions on trade in specific agricultural products are provided for. The Agreements also cover common trade related provisions, including a standstill on trade restrictions, safeguards, antidumping provisions, rules of origin and shortage provisions allowing for export restrictions. 1/

Association Agreements are also under negotiation between the EC and Bulgaria and Romania. An agreement concluded with the former U.S.S.R. in December 1988 provides for the gradual elimination of discriminatory quantitative restrictions (by 1995) but does not envisage the possibility of concluding a follow-up association agreement. A future trade and cooperation agreement with Russia is under discussion.

With the break up of the ex-U.S.S.R. territories, the EC has also begun to formalize its trade relations with the Baltic States and other countries in the former FSU as well as Albania. In February 1992, it initialled trade and cooperation agreements with Estonia, Latvia, Lithuania and Albania. These agreements cover improved access to EC markets for a list of specified products, the removal of specific quantitative restrictions on imports from the Baltic States, and reciprocal MFN treatment on trade as well as broader cooperation. A Joint Committee is to be set up to oversee relations. These agreements are expected to be the first stage of closer relations.

A trade and cooperation agreement was also concluded with the former German Democratic Republic (GDR) in May 1990. Viewed as a transitional arrangement pending full political unification with the former Federal Republic of Germany (which, at the time, was not expected to occur before the end of 1992) the agreement provided for the GDR's adoption of the EC's Common External Tariff on July 1, 1990, and for the simultaneous elimination of all EC customs duties and quantitative restrictions on industrial goods vis-à-vis the GDR. The GDR was absorbed into the Community upon the unification of Germany on October 3, 1990. Since then certain transitional arrangements have applied to the adoption of internal market legislation in the territory of the former GDR (e.g., on product standards), and to trade with the European CMEA countries to permit the former GDR to fulfill contracts concluded with these countries under the state trading system. In particular, the EC is applying transitional measures in the form of tariff quotas and quantitative restrictions limiting imports of industrial products from the CMEA countries to the amounts agreed under the GDR's bilateral contracts, with the understanding that imports under these contracts would

1/ The EC has subsequently curtailed steel imports from Czechoslovakia under the safeguard clause.

remain in the territory of the former GDR. The CAP applies to imports of agricultural products into the territory of the former GDR from CMEA countries. In December 1990, the GATT had granted a waiver for the transitional measures applying to former GDR trade, subject, inter alia, to a report on the use of the waiver. The EC submitted such a report in December 1991.

d. Lomé Convention (ACP preferences)

The EC extends duty-free access to its market on a nonreciprocal basis, as well as financial and technical assistance, to 69 African, Caribbean, and Pacific (ACP) countries under the Lomé convention (successor to the Yaoundé Convention), which was first signed in 1976 and, subsequently renewed on three occasions. The most recent agreement, Lomé IV, was signed in December 1989 and will cover the period 1990-2000. The new agreement provides for some ECU 12 billion in EC aid for the ACP countries during 1990-95, compared with ECU 8.5 billion budgeted under Lomé III (1984-89). In addition, repayable advances under the STABEX and SYSMIN systems were converted into grants, 1/ and access for certain ACP exports to the EC market has been improved.

Despite improvements incorporated in the Lomé IV agreement, some ACP countries remain concerned that the trade preferences they currently enjoy will be eroded by the EC's multilateral trade concessions in the Uruguay Round. In view of the limited progress that has been achieved in developing their industrial sectors, despite preferences granted by the EC, some ACP countries also have called on the EC to relax its rules of origin to help promote ACP industrial exports incorporating components manufactured outside the EC and ACP countries. Some Southern European countries, particularly Greece and Italy, have resisted an expansion of trade preferences on products that compete with their own and have instead advocated greater reliance on aid rather than trade preferences. ACP countries are also concerned about the retention of preferences under the single market. This issue has been raised over the treatment of non-ACP banana imports after 1993. The banana protocol was adopted unchanged in Lomé IV; this guarantees ACP suppliers traditional preferences in EC markets. 2/ A supplementary Joint Declaration includes an undertaking by the EC that ACP states will retain their traditional status after the completion of the internal market. These commitments underlie the current dispute with non-ACP banana suppliers--mainly in Central America--over EC market share. The EC Commission has proposed Community-wide quotas for these suppliers, and

1/ The STABEX and SYSMIN systems are intended to help stabilize the ACP countries' export earnings for agricultural and mining products, respectively.

2/ The relevant section in Article 1 of the protocol on bananas reads: "No ACP State shall be placed, as regards access to its traditional markets and its advantages on those markets, in a less favorable position than in the past or at present."

banana-exporting countries--Colombia, Costa Rica, Guatemala, Nicaragua, and Venezuela--have requested consultations with the EC under the GATT on the issue (see Section IV).

e. GSP scheme

The Community's Generalized System of Preferences (GSP) scheme provides duty-free access to the EC market for industrial products exported by developing countries, with certain restrictions on duty free access by product and by country (see below). The coverage of agricultural products is more selective and concessions are more limited; it limits the coverage of products exported by the ACP countries, and concessions usually consist of duty reductions rather than exemptions.

In the mid-term review of the Community's GSP scheme in 1986, provisions were introduced to graduate certain products or countries from the scheme in order to achieve greater differentiation of the preferential advantages among beneficiaries. Countries that have a per capita income exceeding US\$2,000 and whose share of EC industrial imports from nonmembers exceeded 20 percent of the total for the product concerned were graduated from the scheme for industrial products. In 1987, the policy of differentiation was extended to the textiles sector for countries that have a per capita income exceeding US\$2,000 and whose share of EC imports of the product concerned exceeds 10 percent. Since their introduction, these provisions have been applied to exports from Brazil, the People's Republic of China, Hong Kong, Korea, Libya, Saudi Arabia, and Singapore. Benefits are withdrawn over two years, and the benefits withdrawn from one beneficiary are redistributed to other beneficiaries of the scheme. The Czech and Slovak Republics, Hungary and Poland were graduated from the GSP scheme upon implementation of the Association Agreements with them.

Some extensions have been made to the GSP. The EC extended GSP treatment to 23 products or product groups in 1989, including, for the first time, eight products subject to variable levies under the CAP. For the latter products, preferential treatment takes the form of a 50 percent reduction of the levy, within overall quotas. In 1990 and 1991, the European Parliament extended GSP benefits to the Andean countries (Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua, and Panama) and Central America (Bolivia, Colombia, Ecuador, and Peru). The benefits cover some agricultural exports to the community--notably coffee. ^{1/} The 1992 GSP scheme was extended to Estonia, Latvia, Lithuania, and Albania, excluding some fishery products from the Baltics.

^{1/} European Report, December 14, 1991.

IV. Recent Trade Disputes

There has been an unprecedented increase in recourse to GATT's dispute settlement system since 1986 (when the Uruguay Round began), with a surge in the past year. 1/ Twelve GATT panels were requested during 1991 (compared with one in 1990), of which 3 involved EC members. This reflected a number of factors, including the intensification of problems facing world trade in agriculture and trade frictions related to newly emergent sectors, such as electronics and high technology. Increased recourse to GATT panels in recent years may reflect attempts to use the dispute settlement mechanism to test or clarify existing GATT rules or establish areas where new rules are needed. The EC has been an active participant in the dispute settlement system, both in defending its own policies against specific charges and in challenging the GATT legality of various policies of trading partners.

1. Disputes involving EC trade practices

In the area of agricultural disputes, one of the most significant developments in recent years was the establishment of a dispute settlement panel in 1988 to examine a United States complaint about EC subsidies to producers and processors of oilseeds and related animal feed proteins. The panel request followed an "unfair trade" complaint under Section 301 of the 1974 United States Trade Act filed by the American Soybean Association, which alleged that EC subsidies had led to a six-fold increase in EC soybean production over the past 15 years, with a sharp resulting decline in U.S. soybean exports to the EC. The panel's report, which was adopted by the GATT Council in January 1990, found that EC subsidies to purchasers and processors of oilseeds produced in the EC to compensate for the difference between EC target prices and world prices violated GATT rules on national treatment in that they were provided only for the purchase of domestically produced oilseeds. The panel also found that subsidies to oilseed producers nullified and impaired previously negotiated zero tariff bindings on these products. Although the EC did not oppose the GATT Council's adoption of the report, it maintained that at least some of the panel's findings were erroneous; it stated that it will implement the panel's recommendations in light of the Uruguay Round outcome on "rebalancing"--raising tariffs on some imports, such as cereal substitutes, in return for lowering tariffs on some other goods. Since then, the EC has eliminated premiums paid to domestic processors and adopted a proposal to replace the producer price guarantee granted per ton of oilseeds by direct per hectare payments. The United States requested that the panel be reconvened in 1991, on the ground that the remaining subsidy system still constituted nullification and impairment of the zero tariff bindings. In April 1992 the panel again found EC policy

1/ Consultation and dispute settlement procedures are basically governed by Articles XXII and XXIII of the GATT. If bilateral consultations do not result in a settlement, the complainant may request a panel of independent experts to examine the case under Article XXIII:2.

incompatible with the GATT and recommended that the EC either modify the support system or renegotiate its tariff concessions for oilseeds. The EC rejected the panel findings, and the GATT subsequently authorized the EC to renegotiate the EC's tariff concessions for oilseeds and oilcake under Article XXVIII of the GATT. The United States has released a list of imports from the EC on which it proposes to impose substantial retaliatory tariffs if the dispute remains unresolved, and the EC has threatened counter-retaliation. Discussions on the matter are continuing.

Two agricultural disputes with the United States, neither of them yet fully resolved, have concerned the use of standards allegedly to enforce import restrictions on beef. In one case, the United States charged that an EC ban on hormone-treated beef, although ostensibly a public health regulation, was unsupported by scientific evidence and was intended to protect domestic beef producers. ^{1/} The United States requested the GATT Committee on Technical Barriers to Trade to establish a panel of experts to examine the scientific merits of the case, but the EC objected on the grounds that the matter was outside the Committee's competence. Following the entry into force of the hormone ban in early 1989, the United States introduced retaliatory duty increases under Section 301 of the 1974 Trade Act on a number of EC products and subsequently blocked an EC request for the GATT Council to examine the legality of the United States retaliatory action. However, EC plans to counter-retaliate were shelved in February 1989 following the formation of an EC-United States task force to explore possible means to resolve the dispute. The U.S. retaliatory tariff on one of the products (pork) was subsequently lifted following the certification of a number of U.S. meat packers to export non-hormone treated beef to the Community. The adoption of a standard on maximum residue levels of hormones used to promote growth was considered by the Codex Alimentarius Commission in July 1991, but a decision was postponed until its next session in 1993.

In late 1987 a GATT dispute settlement panel was established to examine the EC's Third Country Meat Directive. The United States charged that the Directive was inconsistent with GATT rules on national treatment in that it required non-EC meat exporters to comply with more stringent certification requirements than those imposed on domestic producers. However, the terms of reference of the panel were never drawn up and efforts to get the panel underway were suspended following the resumption of bilateral discussions between the parties to resolve the dispute. In July 1991, the United States requested the establishment of a panel, after the EC delisted remaining U.S. pork plants from those eligible to export to the EC in October 1990, and halted U.S. beef exports in January 1991. Formal procedures have, however, again been halted as bilateral negotiations have continued.

While trade disputes frequently concern import restrictions, a few disputes, mainly involving nonagricultural primary products, have concerned

^{1/} The hormone ban applies to both domestic and imported beef.

export restrictions. 1/ The GATT Council established a dispute panel in July 1989 to examine a long-standing U.S. complaint about EC export restrictions on copper scrap. 2/ The United States alleged that EC copper producers benefitted from the low domestic price of copper scrap, while world market prices were forced up by limited supply. The EC responded that its restrictions were intended to prevent a critical shortage of essential supplies and were therefore a permitted exception to the general prohibition on export restrictions. The dispute was subsequently resolved on the basis of bilateral consultations.

In the area of trade in industrial products, EC antidumping regulations have been an ongoing source of friction. Japan and Hong Kong, among others, have argued that EC procedures governing the calculation of dumping margins are biased in favor of positive dumping findings and involve large margins of error in cases where they are based on estimated production costs and profit margins. 3/ A matter of particular concern to Japan has been the EC "screwdriver" legislation which allows for the imposition of antidumping duties on products assembled in the EC from mainly imported components in cases when imports of the final product concerned had already been subject to antidumping duties (see Section III.2.c). Of the eight investigations initiated pursuant to this legislation since 1988, four resulted in the imposition of definitive antidumping duties, which were later revoked in exchange for minimum price undertakings. Japan considered the duties to be a protectionist device aimed at forcing EC-based affiliates of foreign companies to use components of EC origin, and in 1988 it made its first ever request for the establishment of a GATT dispute panel to examine the EC legislation. The panel found that duties assessed on locally assembled final products violated GATT rules on national treatment. While allowing the GATT Council to adopt the panel report in May 1990, the EC stated that the panel's findings were fundamentally flawed and emphasized that it would implement the panel's recommendations only if a satisfactory solution to the problem of circumvention was agreed in the Uruguay Round.

A distinct but related issue arose in 1989 in connection with product-specific origin rules issued by the Commission, particularly those on photocopiers (which are subject to EC antidumping duties when imported from Japan or assembled by EC affiliates of Japanese companies) and semiconductors. Based on these regulations, photocopiers made in the United States using components imported from Japan were considered of Japanese origin and were subjected to EC antidumping duties. Thus, the origin regulation on photocopiers in effect extended the screwdriver legislation to assembly operations in third countries. Private sector representatives in

1/ Gatt's general prohibition on the use of quantitative restrictions (Article XI:1) pertains to both import and export restrictions.

2/ Another example of a dispute involving export restrictions was a United States complaint about Canadian export restrictions on certain fish.

3/ This view has also been expressed by independent observers. See, for instance, Hindley (1988) and Wolf (1988).

the United States emphasized that the assembly operations were intended to exploit comparative cost advantages rather than circumvent EC antidumping duties.

The EC subsidies to Airbus have been the source of a long-running dispute with the United States. Of particular concern to the United States was the exchange rate insurance scheme for the German aircraft industry--the mechanism that linked German Government subsidies to Deutsche Airbus with the level of the United States dollar/Deutsche mark exchange rate. The United States considered that the exchange rate/subsidy link gave rise to a violation of the GATT Subsidies Code, and requested a panel under the Subsidies Code in February 1991. In January 1992, the Committee on Subsidies and Countervailing Measures of the GATT found that the exchange rate guarantee scheme constituted an export subsidy prohibited by the Code. The exchange rate-subsidy link was subsequently removed. The United States also began bilateral negotiations with the EC over the full range of subsidy schemes to Airbus. By April 1992, preliminary agreement had been reached between U.S. and EC negotiators on these broader U.S. complaints. The agreement rules out production subsidies and establishes maximum support levels for new commercial airline projects, both for direct research and development costs (relevant for Airbus) and indirect aid as in the military and space research contracts to the aircraft industry (relevant for U.S. companies); EC governments will limit subsidies to Airbus.

With the implementation of the single market program, the Commission has proposed to replace different national trade regimes with respect to bananas by an EC-wide regime that would entail a quota and a 20 percent tariff on banana exports to the EC from nonpreferential third countries (mainly in Central America). The aim was to preserve existing ACP preferences (see Section III.4.d). A number of banana exporting countries in Latin America have reacted with concern that the Commission's proposal would discriminate against Central American producers, have requested consultations with the EC over the GATT-consistency of the existing and proposed banana import regimes, and pressed for agreement on free trade in bananas in the Uruguay Round.

Some trade frictions have not been brought to GATT dispute settlement but have been dealt with bilaterally. For example, for a number of years EC steel exports to the United States have been subject to VERs or antidumping/ countervailing duties. Attempts to negotiate a multilateral steel accord were suspended in March 1992. Subsequently, U.S. steel companies filed dumping and countervailing duty petitions against exporters in 21 countries, of which 6 are EC member states.

Among EC practices of concern cited in the United States Trade Representative's 1990 and 1991 Report on Foreign Trade Barriers were: (i) variable import levies, price supports, and export subsidies under the CAP; (ii) "buy national" public procurement policies for public utilities and agencies not covered by the GATT Code on Government Procurement;

(iii) public procurement standards and standard setting procedures that act as a barrier, particularly to United States electricity-generating and telecommunications exports; (iv) insufficient protection of intellectual property rights, particularly in Southern European countries; (v) recent decisions regarding rules of origin that elevated the degree of processing required to confer origin on certain products, such as integrated circuits; (vi) national subsidies to the shipbuilding and coal industries; and (vii) government support for Airbus (see above), and the shipbuilding industry; and (viii) the EC Broadcast Directive which may discriminate against foreign productions. While maintaining support for the process of EC integration, many countries have expressed concern that certain aspects of the internal market program might have adverse implications for their exports of goods and services.

2. Disputes involving the practices of the EC's trading partners

The EC has brought a number of disputes to the GATT in recent years, most involving practices by the United States or Japan. Disputes with the United States have mainly centered around the perceived discrimination against foreign products on the U.S. market arising from internal taxes and regulations. Two such disputes concerned U.S. taxes on petroleum products (in which Canada and Mexico joined the EC as complainants) and the U.S. customs user fee. In the former case, the dispute panel found that U.S. internal taxes on imported petroleum products (used to fund the "Superfund" toxic waste clean-up program) violated GATT rules on national treatment. In the latter case, the panel found that the U.S. customs user fee exceeded the cost of customs services rendered and therefore violated U.S. tariff bindings. Although the United States accepted the GATT Council's adoption of these two panel reports (in June 1987 and February 1988, respectively), frictions persisted for some time after adoption of the reports because the United States did not bring its legislation into conformity with the panels' recommendations until 1990.

In another case, a GATT panel upheld an EC complaint concerning U.S. legislation governing patent protection under Section 337 of the United States Tariff Act of 1930. Specifically, the panel found that differences in legal procedures in patent infringement cases involving imported and domestically produced goods resulted in less favorable treatment being accorded to imported goods, in violation of GATT rules on national treatment. The United States expressed serious reservations about the panel's findings but, after a delay of several months, allowed the GATT Council to adopt the report in November 1989. At the same time, the United States made clear that its ability to enact legislation to implement the panel's recommendations would be enhanced if the Uruguay Round results included enforcement of intellectual property rights.

Two GATT dispute panels have been established at the request of the EC to examine trade practices of Japan. In addition to perceived discrimination against foreign products in Japan's market, these disputes

reflected the EC's concern over the effects of the United States-Japan semiconductor agreement, concluded in 1986, on third countries. Following the conclusion of the semiconductor agreement, which included commitments by Japan to monitor export prices of semiconductors to both the United States and third countries and to increase the domestic market share of imported semiconductors, the EC charged that the agreement violated GATT rules on export restrictions and provided the United States with preferential access to the Japanese semiconductor market. The dispute settlement panel, whose report was adopted by the GATT Council in May 1988, upheld the former, but not the latter, charge. In June 1989, Japan announced that it had implemented the panel's recommendations.

In November 1987, the GATT Council adopted the report of a dispute panel that had investigated an EC complaint about Japanese practices concerning imported alcoholic beverages. The panel upheld the EC charge that Japan's indirect taxes on alcoholic beverages discriminated against imported products, in violation of GATT rules on national treatment, but it rejected the charge that Japanese liquor labeling practices violated GATT rules. While Japan has amended its liquor tax law in light of the panel's recommendations, the EC maintains that the panel's recommendations have not been fully addressed.

The EC has long been concerned with a broad range of perceived trade restrictive practices by local and provincial governments, particularly in countries with federal systems. In 1985 the GATT Council established a dispute settlement panel to examine an EC complaint about alleged discriminatory practices by Canadian provincial liquor marketing agencies. The panel upheld the EC complaint, finding that the application of higher retail mark-ups and the more limited availability of sales outlets for imported alcoholic beverages were inconsistent with GATT principles. The panel further found that the Government of Canada had not taken all reasonable measures to ensure that the practices of the provincial liquor boards were consistent with GATT provisions. The panel report was adopted in early 1988.

The EC has brought few formal complaints about agricultural trade policies. However, in July 1989 a GATT dispute panel was established at the EC's request to examine import restrictions on sugar and sugar-containing products which the United States justified under its 1955 GATT waiver. ^{1/} The panel found that these restrictions were consistent with the terms of that waiver. The GATT Council adopted the report in November 1990.

The EC has become increasingly concerned with the exclusionary impact on trade of U.S. procurement practices, maintaining they involve discrimination in U.S. federal law, fragmentation of markets and structural

^{1/} The United States 1955 GATT waiver concerns import restrictions maintained under Section 22 of the United States Agricultural Adjustment Act, as amended.

impediments, as in telecommunications. In July 1991, the EC brought two cases to the GATT, one on U.S. government procurement of Antarctic research equipment, and one on the United States National Science Foundation's procurement of a sonar mapping system. The panel on sonar mapping submitted its report in April 1992, and it was discussed by the Committee on Government Procurement in May, but had not been adopted by mid-year. In relation to the latter, the panel found that the arrangement concerning the purchase of the sonar mapping system by the United States National Science Foundation did constitute "government procurement" under the Code and was inconsistent with the national treatment obligations of the United States.

A recent case affecting the EC indirectly (but brought to the GATT by Mexico in February 1991) involved a trade embargo by the United States under the Marine Mammal Protection Act of 1972, amended in 1988. The Act establishes dolphin protection standards for the domestic fleet and for countries with vessels catching tuna in the Eastern Tropical Pacific Ocean, where schools of yellowfin tuna often swim beneath schools of dolphins. This case has wider ramifications because it involves both the application of domestic standards to other countries and the use of trade restrictions to enforce such standards, which in this case are environmental. Under the MMPA, imports to the United States of yellowfin tuna products from Mexico (since February 1991) and Venezuela (since April 1991) have been embargoed (the primary embargo) to protect dolphins trapped in purse-seine tuna nets. Since January 1992, as the result of a California court judgment, the embargo has also applied to imports of these products from "intermediary nations" reexporting these goods; this secondary embargo was expanded to cover about 20 countries, including several in the EC. The embargo covers imports of all yellowfin tuna and tuna products from intermediary nations which have not prohibited tuna imports from countries subject to the primary embargo. A GATT panel report of September 1991 found the embargoes violated disciplines against quantitative restraints and could not be justified under exceptions for the protection of animal health and safety or for resource conservation because the species concerned were beyond U.S. territorial jurisdiction. The basis for the finding was that domestic process standards could not be forced on other countries or used unilaterally to restrict trade. The United States was requested to bring the measures into conformity with its obligations.

Adoption of the panel report has not been requested by Mexico, and the United States has pursued the matter bilaterally with Mexico and Venezuela. Both the EC and Japan, however, are seeking its adoption, and three Council debates have been held on the issue in 1992. Meanwhile, the Community has requested consultations with the United States on the secondary embargo under GATT Article XXIII.1. The EC stresses the need to conserve living resources through international cooperation and supports multilateral negotiations as a basis for international rules.

The EC has raised strong objections in various GATT forums to the potential for unilateral actions under Section 301 of the United States Trade and Competitiveness Act of 1988.

V. Industrial Policy Developments

1. Statutory provisions on competition

Industrial policies in the EC are governed by the EEC Treaty of Rome's provisions on competition, contained in Articles 77 and 85 to 94, whose purpose is to limit trade-distorting state aids and business practices within the Community. ^{1/} These provisions prohibit the abuse of dominant market positions--through price fixing and market sharing arrangements, for example--as well as state aids that distort competition and act as a substitute for border protection. Exemptions are granted for state aid to the Community's poorest regions or declining areas, and for schemes in the common European interest (such as aid to Airbus and subsidies for research and development). The rationale for these exemptions is the need to promote convergence of economic performance within the EC, and the need to subsidize projects with high start-up costs that might not otherwise be undertaken. Article 93(3) requires EC member governments to notify the Commission in advance of any plans to grant or alter state aids. The Commission determines whether the aids fall under its jurisdiction under Article 93 and reviews their consistency with EC rules. In the event that the Commission considers that they distort competition within the EC, it may not authorize them or it may recommend changes that would link the aid more closely with restructuring efforts. The Articles in the Treaty of Rome cover noncompetitive behavior related to price discrimination and subsidies within the EC, while the EC's Antidumping and Countervailing Laws apply to nonmember countries. Article 113 of the Treaty of Rome provides for a common commercial policy, although Article 115 allows exceptions for purely national measures (see Section III.3.b.). ^{2/}

The EC Merger Control Regulation (which came into force in September 1990) creates extensive new obligations for the notification of concentrations between large companies that meet certain threshold requirements. (The threshold is currently set at a combined worldwide turnover of merging companies of 5 billion ECUs.) The aim of the Regulation was to prevent the defensive strengthening or emergence of dominant market positions in the EC as internal markets opened up. In its first three months of operation, 12 cases had been notified, and 63 were notified in 1991. The Regulation is to be reviewed in 1992 with the possibility of giving it more veto power; in particular, the threshold turnover level may

^{1/} Article 85 applies to restrictive agreements by firms; Article 86 to monopolistic behavior; and Articles 87-94 to subsidies and activities of public utilities.

^{2/} See Kelly et al. (1992).

be reduced to bring more companies within its purview. The extent of extraterritorial powers in the directive has the potential to create conflict between the Commission and other competition authorities. 1/

State aids to coal and steel are governed by separate provisions, included in the ECSC Treaty. 2/ In theory, these provisions are stricter than those included in the EEC Treaty insofar as they provide for the suspension of all subsidies at the end of a transition period. In practice, subsidies continue to be provided under a safeguard clause included in Article 95 of the ECSC Treaty which permits "appropriate amendments" in the case of unforeseen difficulties at the end of the transition period. In the steel sector, state aids are permitted only in connection with restructuring that leads to capacity reductions, while operating subsidies are banned. The latest revision of the Steel Subsidies Code was published by the EC in December 1991, and is effective January 1992-December 1996. It authorizes subsidies for research, development, environmental protection and factory closures. It also regulates regional aid, extended for the first time to Portugal and the new German Länder. Somewhat looser provisions have generally applied to the coal sector, where noneconomic criteria are explicitly recognized as a valid basis for granting state aid, including improving the security of national supply. More recently, however, the Commission has taken a firmer stand against subsidies to coal, particularly to the German coal industry that is the largest and most heavily subsidized in the EC (see below).

Competition in the shipbuilding sector was governed by a Community directive adopted in early 1987, which expired at the end of 1990. At the same time, a new Directive was adopted, to apply for three years from January 1991 to the end of December 1993. The new Directive limits aid to ship conversions, tightens rules to avoid concentrations of shipbuilding order, and alters monitoring procedures. Operating subsidies are limited to a specified proportion of the contract value and are subject to annual review. The limit, which does not apply to exports to developing countries financed through soft loans, have been reduced substantially since the 1980s. The ceiling on subsidies for 1992 has been fixed at 9 percent of total costs for larger ships, and 4.5 percent for repairs and smaller ships, compared with 13 percent and 9 percent, respectively, in 1991. Within the Community, the limit is intended to promote restructuring by preventing an excessive concentration of subsidies in the least competitive shipyards.

1/ In the United States, the Government can only prevent a proposed merger if it can prove it would be anticompetitive, while under the new rules in the EC, the company must prove a proposed merger would not restrict competition (Julius (1991), p. 2). Under the "reciprocity" clause of the Merger Control Regulation, Article 24, third countries may come under pressure to alter aspects of their competition laws (Canada: Bureau of Competition Policy (1991), p. 20).

2/ Articles 4, 54, and 95 of the ECSC Treaty.

Investment subsidies may be granted only in connection with restructuring that leads to capacity reductions.

2. Implementation of EC competition policy

Although the EC has strict statutory provisions on competition policy, difficulties in enforcing these provisions have frequently arisen. Member governments have not always complied with notification requirements for state aids--145 out of 617 cases recorded in 1991 were not notified--and sector-specific aid has sometimes been provided under the guise of regional or social policy which is sanctioned by EC rules. The implementation of competition policy is further complicated by difficulties in assessing compliance with EC rules, particularly as regards state-owned enterprises. EC rules require member governments to behave like commercial investors when providing equity to state-owned enterprises, but it is not always clear in practice how private investors might act. Similar difficulties arise in assessing whether regional aid is more than sufficient to overcome locational disadvantages.

The enforcement of EC competition policy has become considerably more strict since the single market program was launched in 1985, with the objective of establishing a "level playing field" within the EC. The intensification of enforcement efforts reflects the recognition that the removal of internal barriers could compound existing distortions in trade and investment flows arising from different degrees of subsidization within the Community. This recognition was facilitated by budgetary considerations at a time when several EC countries were aiming at fiscal consolidation, which in turn created pressures from some members for greater control over trade-distorting subsidies provided by other members. Two additional contributing factors were the disappointing performance of the beneficiaries of large-scale assistance and the fact that sector-specific subsidies are frequently countervailed by trading partners outside the EC.

The stricter enforcement of EC competition rules since 1985 is apparent in five main areas. First, the procedures applied in cases of non-notified aids were tightened. The procedures providing for a termination of state aids incompatible with EC competition rules under Article 93(2) are now opened automatically if a member fails to respond to the Commission's request for notification within a limited time period.

Second, the Commission systematically demands that non-notified aids be reimbursed. Demands for reimbursement jumped from ECU 11 million in 1986 to ECU 747 million in 1987, and have remained high in subsequent years.

Third, the transparency of EC procedures and practices was increased substantially. To encourage the intervention of interested third parties, all decisions on state aids issued by the Commission--whether positive or negative--are now published in the EC Official Journal. Moreover, the

Commission has started compiling a survey of state aids provided by EC countries (see sub-section 3 below).

Fourth, stricter rules for the EC automobile industry came into effect for a two-year period starting on January 1, 1989. Under the new rules, member governments must obtain advance clearance from the Commission for all state aids to the automobile industry exceeding ECU 12 million, regardless of whether the grant is a new scheme or additional funding for schemes already approved by the Commission, including regional schemes. Moreover, the Commission has launched an investigation into regional schemes maintained by member countries that may favor the automobile industry in cases where it is geographically concentrated in a region that benefits from such schemes.

Fifth, as noted above, EC-wide rules on mergers and acquisitions have been developed in the context of the internal market program (see Section II). This is intended to strengthen existing rules prohibiting the abuse of a dominant market position through cartelization of markets.

In July 1989, the Commission launched a major review of existing aid schemes, including those approved by the Commission in the past, to assess the need for their continued existence in light of restructuring efforts and changes in market conditions that may have occurred since their approval. As a result of such an investigation, Renault agreed in May 1990 to repay 50 percent of FF 12 billion in subsidies granted in 1988. Likewise, British Aerospace was to repay US\$44 million in subsidies granted in conjunction with the company's purchase of Rover in 1988. In other cases, the Commission has approved continued aid where such aid was closely linked to adjustment efforts. For example, the Commission has sanctioned continued aid to the German coal industry until 1995, in view of the program introduced in 1991 to reduce mining capacity and employment in the sector between 1995 and 2000. 1/

Stepped-up enforcement has also extended to the area of mergers and acquisitions. In June 1990, the Commission initiated formal complaint procedures against a joint venture agreement involving a plan by Sabena, KLM, and British Airways to combine their operations out of Brussels. 2/ Similarly, in February 1990, the Commission sent a statement of objection to Air France regarding its takeover of UTA Airlines, alleging that this constituted a prima facie abuse of a dominant position.

1/ Subsidies to the coal industry in Germany are provided through marketing programs designed to compensate the users of German coal (mainly the electricity industry) for the difference between the German price of coal and the world market price of coal and other energy sources. A detailed discussion of the German coal industry is contained in Lipschitz et al. (1989).

2/ The agreement resulted in the formation of Sabena World Airlines, which has operated Sabena's international flights since January 1, 1990.

The most recent EC Report on Competition Policy (for 1991) reviews the first 12 notifications of mergers since the new Regulation on mergers entered into force in September 1990. One was judged to be not applicable and the others compatible with the common market. The unification of Germany raised special issues; for example, existing monopolies in the former German Democratic Republic needed to be dismantled and powerful firms in West Germany prevented from establishing dominant positions. The Commission investigated and monitored a number of cases to ensure that this did not happen. The Commission also continued a stricter application of competition rules, particularly in state regulated markets such as telecommunications, postal services and energy. In a case involving the Régie des Télégraphes et Téléphones (RTT) in Belgium, for example, the RTT agreed to stop applying restrictions that the Commission considered liable to affect competition.

During 1991 the Commission received 63 notifications under the Merger Control Regulation, and took 60 final decisions. In the great majority (50 cases) the mergers were found to be compatible with the common market. In the detailed investigation of 6 cases, mergers were authorized in 3 (Alcatel/Telettra, CEAC/Magneti Marelli and Varta/Bosch) subject to conditions, and in one case--Aerospatiale-Alenia/de Havilland--the proposed takeover by the Franco-Italian consortium was found incompatible with the Common Market and was vetoed. Other actions were taken to remove rules and regulations impeding free competition within the EC, affecting particularly insurance, telecommunications (see Section II.2.b) and air transport. In an effort to extend the application of its principles of competition policy, the EC has signed a cooperation agreement with the United States antitrust authorities. Implementation is pending subject to a revision of the proposed legal controls. The Association Agreements concluded with Czechoslovakia, Hungary and Poland allow for a phased application of competition policies similar to those applied in the EC.

3. Survey of state aids in the EC

As part of its effort to increase the transparency of state aids, the Commission issued a First Survey of State Aids in the EC in December 1988, followed by a Second Survey in July 1990, and a Third Survey in July 1992. 1/ The surveys focused on aids to manufacturing, agriculture, rail transport, and coal mining. The level of assistance has fallen gradually

1/ The surveys cover the following types of subsidies: (a) budgetary grants; (b) soft loans and loan guarantees; (c) government funding of research and development schemes of private or state enterprises; (d) tax credits, allowances, exemptions, and reliefs; (e) reductions in social security contributions; and (f) equity participation (including conversion of debt to equity) by the public authorities in private or public enterprises. Only the aid element of state aids is included in the figures. The data for some sectors in certain countries are estimates. The data on Greece are highly tentative.

over the decade. The first survey estimated the volume of subsidies provided through the EC and national budgets at ECU 109 billion (in 1987 prices) per year in 1981-86, equivalent to 2.8 percent of the Community's GDP. The second survey, covering the period 1986-88, showed a decline in state aids to 2.2 percent of GDP, while the third shows a fall to 2 percent of GDP for 1988-90. Disparities among countries are wide. National percentages varied from less than 1.5 percent of GDP in Denmark, the Netherlands and the United Kingdom to more than 2.5 percent in Belgium, Greece, Italy and Luxembourg (Table 11). In terms of ECU per person employed, Luxembourg, Belgium, Germany, and Italy spent over three times the amount spent by Portugal and the United Kingdom (Table 11).

The focus of assistance also varied widely both across sectors and countries. The most heavily subsidized subsectors were shipbuilding, railways, and coalmining. In terms of shares of sectoral value added, Italy, Portugal, Denmark, and France strongly assisted shipbuilding, while railways and coalmining were heavily supported by Belgium, Germany, France, Luxembourg, and Spain (Table 12). Agriculture was considerably more heavily subsidized through state aid than manufacturing, except in Greece, Ireland, and Spain. Aids to agriculture ranged from less than 2 percent of sectoral value added in Spain to more than 15 percent in Germany and Luxembourg. Agriculture also received substantial support (not included in the data) through the EC budget and EC consumers, which far outweighed national support to this sector. Aid to the manufacturing sector averaged 3.5 percent of manufacturing value added, ranging from less than 3 percent in Denmark, Germany, Luxembourg, and the United Kingdom to almost 5 percent in Italy, Portugal, and Ireland. Most countries concentrated their aid to manufacturing in transport and declining sectors such as coalmining (the United Kingdom, Germany, and Belgium), shipbuilding (Portugal and Denmark), or steel (Portugal and Spain) (Table 11). Excluding these sectors, most countries allocated a higher share of aid to agriculture.

By type of subsidy, budgetary grants accounted for the bulk of national state aids in all EC countries (Table 13). Tax reductions were a common form of assistance in Germany, Ireland, and Italy which provided at least 18 percent of their national subsidies in this form. Equity participations were 40 percent of the total in Portugal. Soft loans accounted for a larger share of total assistance in Denmark, France, Greece, and Spain than in other member states. 1/ Loan guarantees accounted for over 10 percent of total assistance in France, but were negligible in other EC countries.

State aid has generally fallen in the EC in constant prices. Comparing 1986-88 with 1988-90 averages, assistance has dropped by 2 percentage points of value added in transport, with all the large-subsidy countries spending a lower share. Aid to shipbuilding has shown less of a decline. The shares of sectoral value added represented by the subsidies are nevertheless very

1/ The shipbuilding sector accounted for almost all soft loans in Denmark.

high in these sectors in some countries--for transport over 50 percent in the Benelux countries, and over 25 percent in Germany, Spain, and France, and for shipbuilding over 50 percent in Italy, Portugal, Denmark, and France. Still in terms of sectoral value added, agricultural aid has fallen slightly (based on national aid data), both on average and in most countries, but rose on the basis of a measure including Community aid. According to this measure, Germany has the highest share--about 20 percent--with Italy, Portugal, the United Kingdom, Luxembourg, and Ireland with shares over 10 percent of value added.

The overall trend in EC aid to manufacturing shows a 9 percent decline between 1986-88 and 1988-90. In percent of sectoral value added, the decline is from 4.0 percent to 3.5 percent. In general, countries with above average levels of aid to the sector (apart from Italy) reduced their subsidies, Spain by as much as 44 percent. Several countries, however, including Portugal and the Netherlands, increased state aid substantially. In terms of value added, Italy, Portugal, Ireland, and Belgium still have shares above 4 percent compared with the United Kingdom that has a 2 percent share. (The data for Greece are not comparable.)

VI. Summary and Conclusions

The Treaty of Rome identified as one of its principal objectives the free movement of goods, services, labor and capital within the EC. Early efforts focused on obstacles to trade in goods, and by 1968 internal customs duties had been eliminated and a common external tariff established. While this provided a tremendous boost to the expansion of intra-EC trade, internal markets for goods and services continued to be segmented. The first revision to the Treaty of Rome--the Single European Act of 1987--was a major step to removing remaining internal barriers, aiming to create a single market in goods, services and factors of production by the end of 1992. Over 90 percent of the proposals in the Commission's 1985 White Paper on the Completion of the Internal Market had been officially adopted or agreed at the political level by mid-1992. These aim to remove remaining border measures, technical barriers to trade, discriminatory public procurement practices and national restrictions on third country imports. Markets for services are to be liberalized; financial services, transport and telecommunications are being opened to foreign competition. Banking, investment services, and non-life insurance have progressed farthest, with EC-wide banking to enter into force at the same time as the single market program. Domestic competition policies are to be harmonized to maximize the benefits of economies of scale in the large internal market. Steps are also being taken to harmonize working conditions and to increase labor mobility--such as through the mutual recognition of academic degrees. Consistent with the aim of the Treaty of Rome to eliminate trade-distorting business practices and state aids within the EC, recent industrial measures--described in Section V--prohibit the abuse of dominant market positions and act to control state aids that distort competition and substitute for border

protection. Capital controls are being fully liberalized by member states and all exchange controls are to be lifted by the end of 1992. With the completion of the single market program in sight, a further boost will be given to intra-EC trade and investment and competitiveness in external markets will be enhanced.

The EC's current external trade regime is characterized by relatively low tariffs on industrial products with a significant proportion bound in the GATT. The most important non-tariff measures affecting trade in goods with third countries include voluntary export restraints (VERs), rules of origin requirements and the CAP. Use of antidumping instruments has also sometimes operated as a source of contingent protection. Article 115 of the Treaty of Rome permits restriction of imports from third countries passing through other EC members. While recourse to this instrument has declined over time, its renewal in the Maastricht Treaty of December 1991 leaves open the possibility of its potentially restrictive use and contradicts the spirit of the single market program. An important aspect of the EC's external trade regime is the extensive network of preferential and nonreciprocal trade arrangements. It currently has 24 different trade arrangements covering trade with 150 countries; under the Lomé Convention alone, 69 developing countries have duty-free access to EC markets. The EC's common external regime after 1992 is still evolving. In principle remaining national restrictions are to be replaced by EC-wide measures. Recent attempts to forge EC-wide policies on auto and banana imports point to continued reliance on managed trade in industry and agriculture. The proposed quotas on bananas, for example, while aiming to safeguard access of preference receiving countries in the ACP, could be detrimental to other agricultural exporters, just at a time when the Uruguay Round is trying to bring agriculture under GATT disciplines and replace quotas by tariffs.

The review of EC trade and trade-related industrial policies finds that in some instances, as with large segments of the agriculture, textiles and clothing, and automobile sectors, the pursuit of domestic producer interests has resulted in the implementation of essentially defensive policies that seek to protect employment in inefficient or declining sectors, at the expense of consumers and efficient producers both within and outside the EC. In other instances, it has resulted in trade liberalization within the Community itself and through trade agreements with other countries. Trade disputes involving the EC, have also largely followed the interests of protected sectors, being concentrated in sensitive and emerging sectors in agriculture and industry and in such practices as government procurement. The increase in the use of GATT's dispute settlement mechanism by the EC (as well as other industrial countries) may also reflect attempts to test or clarify GATT rules or establish the need for new regulations under the Uruguay Round. At the same time, the nonimplementation of some important panel findings by the EC (and other industrial countries) undermines the GATT at a delicate juncture.

There is considerable scope for trade and domestic support policies in the EC to accelerate structural reform in agriculture and industry. In agriculture, the CAP reforms agreed at the political level by EC Agricultural Ministers in May 1992 aim at increasing the role of market prices in agriculture, and shifting away from price support towards direct income support. While this is an important step toward reducing agricultural distortions in the next three years, the reform process will need to be sustained and strengthened over the longer term. The CAP reforms have helped narrow outstanding differences between the EC and its trading partners on agricultural trade negotiations in the Uruguay Round, particularly regarding internal support, but important issues remained to be resolved (at the time of writing) including with respect to export subsidies and market access. In the industrial sector, although there has been some progress toward restructuring, there is continued need for adjustment in sensitive sectors (such as steel, textiles and clothing, and cars) that are currently sheltered by VERs, extensive antidumping actions or other restrictive trade measures. The enforcement of EC competition policy has, however, become stricter since 1985 and large mergers and acquisitions are being investigated more forcefully. State aids are being subject to greater scrutiny with a view to limiting their use and tying it more vigorously to structural adjustment measures; according to the most recent survey, state aids have shown a decline, although sensitive and declining sectors remain highly subsidized in several EC member states.

A factor that has hampered the pace of external liberalization is the view in some quarters within the EC that protection is a legitimate instrument to insulate sensitive and/or strategic sectors from international market forces. The CAP was designed, in part, to offset changes in external competitiveness through variable import levies with a view to greater internal price stability and preservation of farm incomes. The protection of industries whose survival is deemed important--whether for employment, strategic, or regional development motives--has led to subsidies to domestic producers in the airplane industry, and to the shipbuilding, steel, and coal sectors. Similar motivation underlies VERs protecting car manufacturing and high technology industries. These practices protect large segments of the economy and push the burden of adjustment to unprotected, efficient sectors. The trade-distorting effects of EC subsidies have been raised repeatedly by trading partners, especially in relation to agriculture, the aircraft industry, and steel.

A cornerstone of EC policies regarding foreign trade in goods and services has been the principle of reciprocity, both bilaterally through reciprocal market-opening measures in the context of the internal market program and multilaterally in the context of the Uruguay Round. Depending on their nature and scope, reciprocity provisions may help achieve far-reaching liberalization, both in the EC and the rest of the world. However, the policy of reciprocal liberalization of external trade is not without risks. If mutually agreeable deals cannot be struck, liberalization may not take place. In the context of intra-EC liberalization of banking services,

for example, the single banking license authorizing banks to operate in all EC countries may not be granted to new subsidiaries of banks from countries not granting "comparable treatment" to EC banks. The results, both in terms of global welfare and EC welfare, could be worse than if the EC were to pursue a more active policy of unilateral liberalization. Another risk is that this policy opens the door to reciprocity in the form of targeted foreign market shares for EC producers, in exchange for the removal of restrictions maintained by EC countries. This form of reciprocity has been proposed, for example, in the Uruguay Round negotiations over the opening of the EC public procurement market. An excessive focus on such a "results-oriented" sectoral approach to trade would promote managed trade.

A liberal external regime after 1992 is essential for the EC to reap the full real income gains that could result from the internal market program. 1/ Protection distorts relative prices and inhibits domestic growth while inviting retaliation from trading partners. Resource allocation in the Community would benefit from increased competition from abroad while open external policies would help pass on to foreign countries the benefits of EC real income gains resulting from the internal market program. The benefits from the internal market program would be enhanced if accompanied by supporting policies to reduce border and nonborder protection against third countries. The coincidence of the EC internal market program with the Uruguay Round provides a unique opportunity to lower trade barriers worldwide and thereby reduce the potential for the diversion of trade and investment.

The perceived benefits of more open internal trade on the single market program and the collapse of the former Soviet Union (FSU) have led more countries to seek closer links with the EC. The former German Democratic Republic became part of the EC when Germany was unified. Austria, Sweden, Finland, and Switzerland have formally applied for accession. Meanwhile, the creation of an European Economic Area (EEA) has been agreed--though not yet ratified by national governments--between the EC and EFTA. Tariff-free trade in industrial goods already exists within the area, hence there may not be much room for further significant trade creation as a result of the EEA; in some instances there is a risk that it may be trade diverting as imports from more efficient foreign producers are replaced by more expensive goods from within the EC. Trade agreements have also been signed between the EC and a number of East European countries. With the Association Agreements with Czechoslovakia (as it then was), Hungary and Poland, and embryonic agreements with the FSU, the benefits of a wider potential free trade area could be--if major distortions within the EC such as those in the agricultural sector are removed--a source of strong potential growth as these countries move toward more market-oriented policies. However, the exclusion of "sensitive" sectors from the Association Agreements with East

1/ Numerous studies have attempted to quantify the effect of the EC and of the single market program. For recent summaries of the literature, see de la Torre and Kelly (1992), and World Bank (1992(b)).

European countries, particularly agriculture, textiles and steel, indicates the preference of the EC for a cautious, gradual approach to liberalization. Furthermore, the pace of EC enlargement may be affected by the EC's current preoccupation with issues related to the monetary union. The impact of the enlargement of the EC as it extends its trading links to new members depends on whether internal distortions are maintained and extended to new entrants, or whether full internal and external liberalization will lead to net trade creation.

The future course of EC trade policies will be influenced by the outcome of the Uruguay Round. Depending on the final compromises struck among participants, the Round could result in some tolerance of existing practices whose GATT legality has been challenged or not fully tested. Under the proposed Draft Final Act (DFA), for example, VERs will be phased out only after four years, with the Community's VER on Japanese auto imports sanctioned for longer. On the other hand, significant internal policy reforms may be required in the EC (and other countries) if the DFA is adopted. This is most obviously the case with agriculture, where EC policies are particularly restrictive. The outcome of the Round will also be instrumental in shaping the EC's external regime after 1992, particularly in new areas, such as services, where unresolved issues overlap with those under negotiation in the Uruguay Round. A successful conclusion of the Uruguay Round, by encouraging reforms in sectors such as agriculture and textiles, could also reduce the potential for trade diversion in an enlarged EC.

Political Agreement on CAP Reform 1/

(Council of Ministers of May 18, 19, 20, 21, 1992)

I. Cereals

1. Prices

The target price for cereals is set at 130 ECU/t for 1993/94, 120 ECU/t for 1994/95, 110 ECU/t for 1995/96 (-29 percent with regard to the prices of the 1991-92 campaign). The intervention price is fixed for the same marketing years respectively at 117, 108, and 100 ECU/t.

2. Compensatory payments for the price reductions

The payments will be on a per hectare basis on the basis of the regional average yield. The basic amount for the compensatory payment is fixed at 25, 35, and 45 ECUs/t respectively for the aforementioned marketing years. When there is an excess of the regional base area (average of the areas per region given over to cereals, oilseeds and protein products cultivated in 1989, 1990, and 1991), the eligible area per producer will be reduced proportionally during the same marketing year. Besides the percentage by which the regional base area is exceeded will be covered, without compensation, by special set aside measures in the following marketing year.

3. Set-aside

In order to benefit from these compensatory payments the farmers producing more than 92 tons of cereals per year must set aside, on the basis of a rotation, 15 percent of their areas given over to cereals, oilseeds and protein products. All these farms will benefit for the area set aside a compensation equal to the compensatory payments per hectare for the reduction of the prices. Producers may opt to apply for a nonrotational system of set aside, but at a higher rate than the rate of 15 percent decided for the rotational system of set aside. The rate will be proposed to the Council by the Commission on the basis of a scientific study. The council will decide on the basis of the proposition before July 31, 1993. Where national environmental rules have the implication that a producer who set aside some of his arable land would thereby be forced to reduce his animal production, such a producer may arrange to transfer his set aside obligation to another producer. His right to compensation would depend on the full performance of that obligation by the farmer to whom it had been transferred. If the transfer is to a different yield area, the amount of set aside to be performed would be adjusted accordingly. Such transferred obligation should, of their nature, be nonrotational, and hence would be subject to the general rules of nonrotational set aside.

1/ This Appendix is a reproduction of the EC press release in May 1992.

4. Community preference

The difference between the threshold price and the target price will be 45 ECU.

5. Cereals for silage

Cereals grown for silage are treated like other cereals.

6. Coresponsibility levies

The coresponsibility levies are withdrawn for the marketing years 1992/93, 1993/94, 1994/95, 1995/96 as well as the two alternative aid schemes for the small producers, that are linked to these levies.

II. Oilseeds and Protein Crops

1. Oilseeds

The principles underlying future arrangements for oilseeds, as proposed in the context of the arrangements for arable crops, are accepted, but the Council asks the SCA to draw up necessary technical amendments taking account of the arrangements in force for 1992/93. Until the end of the 1994/95 marketing year, the aid paid to nonprofessional producers of sunflower seeds in Spain and Portugal will be fixed in such a way as to avoid any distortion which might arise from transitional arrangements for sunflower seed producers in these countries.

2. Protein crops

The aid per hectare of protein crops (peas, beans, and sweet lupines) is 65 ECU/t multiplied by the regional yield for other cereals (excluding maize yields in member states where there is a separate regionalization for maize).

3. Other protein crops

The aid regime for lentils, chick peas, and vetones shall be extended to 1995/96.

III. Milk

1. Quotas

The Commission will submit reports to the Council before the beginning of the 1993/94 and 1994/95 quota periods on the market situation, accompanied, as appropriate, with proposals, so as to allow the Council to

review the decisions taken. The Council is invited to take a decision of principal that if it received satisfactory proof that the quota system has been effectively applied in 1992/93 in Spain and Greece and that production has therefore been reduced, some adaptation in the global guaranteed quantities of these member states will be agreed for 1993/94 onwards (500,000 tons for Spain and 100,000 tons for Greece).

For the marketing year 1992/93, no quota reductions. Butter price reductions by 2.5 percent per year are limited to the two marketing years 1993/94, and 1994/95. The prices for skim milk powder remain unchanged. These decisions will be reviewed annually in the light of market developments. The proposed dairy cow premium is suppressed. The final date for the leasing quota will be December 31.

2. Consolidation and simplification

The regime which shall be applicable from 1993/94 shall be decided upon by the Council before the end of 1992 on the basis of the Commission's proposals.

IV. Beef

1. Price

The intervention price is reduced by 15 percent. This price reduction will be introduced in three equal steps (-5 percent for the marketing year 1993/94, -5 percent for 1994/95, and -5 percent for 1995/96).

2. Premium arrangements

Male bovine animals

A Regional Reference Herd, equal to the number of premiums paid in the reference year, shall be established for each region within member states. Member states may choose as the reference year 1990, 1991, or 1992. A region shall be understood to be a member state or region within a Member State at the option of the Member State concerned. If, in a given region, the number of premium requests exceeds the Regional Reference Herd level, the number of eligible animals per producer shall be reduced proportionately. A premium for young bovine animals shall be fixed at 90 ECU, paid at most twice in the life of an animal: once it has reached 12 months and again after it has reached 22 months. The premium will be phased in three steps as follows: 60 ECUs in 1993-94, 75 ECUs in 1994/95, and 90 ECUs in 1995/96.

Suckler cows

The rights to the suckler cow premium shall be limited for each producer to the number of premiums paid in 1990, 1991, or 1992. Suckler cow premium: 120 ECU. The premium will be phased in three steps as follows: 70 ECUs in 1993-94, 85 ECUs in 1994/95, and 120 ECUs in 1995-96.

Calf conversion premiums

Member states, in the light of their production structures, shall apply: a processing/marketing premium (100 ECU/ a head) for the early disposal of young (8-10 days) male calves from dairy herds; or, for a transitional period of three years, carcasses with a weight between 150 kg and 50 kg, may be accepted for intervention.

Extensification premium

Premiums payable to male bovine animals and suckler cows are increased by 30 ECU per head on holdings where producers can prove that their stocking density throughout the year is less than 1.4 UGB per forage hectare.

The density factor

A density factor shall be fixed at a flat rate of 2 livestock units per hectare, applicable from 1996. During the transitional period, the density factor shall be introduced as follows: 1993, 3.5 units/ha; 1994, 3 units/ha; and 1995, 2.5 units/ha. In calculating the density factor, account shall be taken of all the animals per farm for which premiums are requested (male bovine animals, suckler cows, and sheep) and the number of dairy cattle needed to produce the milk reference quantity attributed to the holding. Clause for small holdings for the two types of premium: 15 livestock units.

Interventions

The following ceilings on intervention purchases will be fixed: 1993, 750,000 tons; 1994, 650,000 tons; 1995, 550,000 tons; 1996, 400,000 tons; and 1997, 350,000 tons.

V. Sheepmeat

The ewe-premium will be granted within the individual producer's headage limits: mountain and less-favored regions, 1,000 head; other regions, 500 head. Fifty percent premiums are payable beyond these limits. Member states may choose either 1989, 1990, or 1991 as the reference year for the premium.

VI. Tobacco

Maximum guaranteed quantities: 1992, status quo (\pm 400,000 tons); 1993, 370,000 tons; and 1994-97, 350,000 tons.

VII. Accompanying measures

Environmental protection (obligatory at the level of the Member States). Aid of 250 ECU/ha and 210 ECU per livestock unit to encourage farmers to use production methods that are better compatible with the environmental requirements. Aid of 250 ECU/ha to conserve or re-establish the diversity and quality of the rural environment. Aid of 700 ECU/ha per year for the set aside of agricultural land for a period of 20 years for the creation of biotopes, natural parks, etc. Afforestation (obligatory at the level of the Member States). Aids for reforestation of 3,000 ECU/ha for coniferous trees and of 4,000 ECU/ha for broad-leaved trees. Aids over a period of five years for the maintenance of areas for reforestation of 900 ECU/ha and of 1,900 ECU/ha respectively. Aid of 600 ECU/ha per year over a period of 20 years to compensate for the loss of income foregone by farmers pending maturity of the trees. This last aid is of 150 ECU/ha for the nonfarmers. Early retirement (optional at the level of the Member States). The early retirement premium will be reserved for farmers aged 55 or more. A fixed amount of 4,000 ECU per year is foreseen plus a variable amount of 250 ECU/ha to a maximum total eligible amount per beneficiary of 10,000 ECU a year.

Table 1. European Community: Share in World Trade

	1960	1970	1980	1988	1989	1990	1991	EC(12)			
								1988	1989	1990	1991
<u>(In percent of world exports)</u>											
Exports											
EC(10) ^{1/}	32.5	40.1	36.3	37.7	37.1	38.9	37.5	39.6	39.1	41.0	39.6
Intra-EC	12.2	19.8	19.4	20.6	20.2	21.4	20.9	23.5	23.3	24.9	24.4
To third countries	20.3	20.3	16.9	17.0	16.8	17.5	16.6	16.0	15.8	16.2	15.2
EFTA ^{2/}	5.8	7.0	6.1	6.6	6.4	6.7	6.3	...	...	...	...
United States	15.9	15.3	12.0	11.9	12.5	11.8	12.2	...	...	...	...
Japan	3.1	6.8	7.1	9.8	9.4	8.6	9.1	...	...	...	...
Developing countries	21.3	19.2	31.9	26.3	26.9	26.6	27.7	...	...	...	...
Asian NIEs	1.6	2.2	4.1	8.3	8.4	8.6	8.6	...	...	...	...
<u>(In percent of world imports)</u>											
Imports											
EC(10) ^{1/}	32.8	39.9	41.2	36.2	35.9	37.9	37.4	39.0	38.9	41.1	40.9
Intra-EC	11.5	19.0	19.9	19.7	19.3	20.5	20.0	22.5	22.3	23.8	23.8
From third countries	21.3	20.9	21.3	16.5	16.6	17.4	17.4	16.5	16.7	17.3	17.2
EFTA ^{2/}	6.6	7.9	7.2	6.6	6.5	6.6	6.0	...	...	...	...
United States	10.8	14.4	14.5	16.6	16.4	15.0	14.2	...	...	...	...
Japan	3.2	6.4	8.0	6.8	7.0	6.8	6.6	...	...	...	...
Developing countries	21.4	18.7	26.3	25.4	25.4	25.3	27.3	...	...	...	...
Asian NIEs	2.1	3.0	5.0	7.5	7.8	8.6	8.6	...	...	...	...

Source: International Monetary Fund, Direction of Trade, various issues. NIEs=Newly Industrialized Economies.

^{1/} Includes the original six EC members plus Denmark, Greece, Ireland, and the United Kingdom. The same group of countries is maintained throughout the period to avoid distortions arising from EC enlargement.

^{2/} Includes the present six EFTA members throughout the period.

Table 2. European Community: Level and Direction of Trade

	1960	1970	1980	1988	1989	1990	1991	EC(12)			
								1988	1989	1990	1991
(In billions of U.S. dollars)											
Exports											
EC(10) 1/	42.2	113.3	665.9	1013.4	1079.2	1295.2	1291.0	1064.6	1137.4	1366.8	1364.4
Intra-EC	16.2	56.6	356.5	555.2	589.5	713.3	719.4	633.1	678.8	828.2	841.3
To third countries	26.0	56.7	309.4	458.2	489.6	582.0	571.7	431.5	458.7	538.6	523.1
Of which:											
EFTA 2/	5.4	13.4	71.5	110.5	115.2	136.2	129.8	113.4	118.3	140.3	133.8
United States	3.5	9.3	37.0	80.8	81.7	92.4	83.9	84.6	85.7	96.5	87.4
Japan	0.3	1.4	6.4	19.3	22.5	27.9	26.5	19.9	23.2	28.7	27.4
Developing countries	12.9	23.8	146.3	158.2	170.5	205.9	213.7	165.7	178.4	214.9	223.3
Asian NIEs	0.4	1.1	7.9	21.2	23.6	28.5	30.6	21.8	24.2	29.2	31.3
Imports											
EC(10) 1/	45.6	118.5	729.1	1004.9	1077.3	1303.7	1340.6	1082.8	1167.7	1416.4	1468.8
Intra-EC	16.3	57.4	352.3	547.7	580.1	705.6	717.1	624.5	667.7	820.1	853.5
From third countries	29.3	61.1	376.8	457.3	497.2	598.1	623.5	458.3	500.0	596.4	615.3
Of which:											
EFTA 2/	4.3	10.5	64.4	102.6	107.8	131.9	131.9	107.1	113.0	138.0	138.7
United States	5.8	12.4	60.8	73.3	83.9	96.8	104.9	79.4	91.2	105.0	111.8
Japan	0.4	1.9	18.6	46.5	48.6	56.2	61.2	50.2	52.6	60.8	65.2
Developing countries	13.5	26.8	186.5	162.3	179.6	218.1	229.2	177.4	197.1	238.9	248.7
Asian NIEs	0.3	0.9	13.1	29.5	30.1	34.5	38.8	31.2	32.0	36.7	42.0
(In percent of EC exports)											
Exports											
EC(10) 1/	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Intra-EC	38.4	50.0	53.5	54.8	54.6	55.1	55.7	59.5	59.7	60.6	61.7
To third countries	61.6	50.0	46.5	45.2	45.4	44.9	44.3	40.5	40.3	39.4	38.3
Of which:											
EFTA 2/	12.8	11.8	10.7	10.9	10.7	10.5	10.1	10.6	10.4	10.3	9.8
United States	8.3	8.2	5.6	8.0	7.6	7.1	6.5	7.9	7.5	7.1	6.4
Japan	0.7	1.2	1.0	1.9	2.1	2.2	2.1	1.9	2.0	2.1	2.0
Developing countries	30.6	21.0	22.0	15.6	15.8	15.9	16.6	15.6	15.7	15.7	16.4
Asian NIEs	0.9	1.0	1.2	2.1	2.2	2.2	2.4	2.0	2.1	2.1	2.3
(In percent of EC imports)											
Imports											
EC(10) 1/	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Intra-EC	35.7	48.4	48.3	54.5	53.8	54.1	53.5	57.7	57.2	57.9	58.1
From third countries	64.3	51.6	51.7	45.5	46.2	45.9	46.5	42.3	42.8	42.1	41.9
Of which:											
EFTA 2/	9.4	8.9	8.8	10.2	10.0	10.1	9.8	9.9	9.7	9.7	9.4
United States	12.7	10.5	8.3	7.3	7.8	7.4	7.8	7.3	7.8	7.4	7.6
Japan	0.9	1.6	2.5	4.6	4.5	4.3	4.6	4.6	4.5	4.3	4.4
Developing countries	29.6	22.6	25.6	16.2	16.7	16.7	17.1	16.4	16.9	16.9	16.9
Asian NIEs	0.7	0.8	1.8	2.9	2.8	2.6	2.9	2.9	2.7	2.6	2.9

Source: International Monetary Fund, Direction of Trade, various issues. NIEs=Newly Industrialized Economies.

1/ Includes the original six EC members plus Denmark, Greece, Ireland, and the United Kingdom. The same group of countries is maintained throughout the period to avoid distortions arising from EC enlargement.

2/ Includes the present six EFTA members throughout the period.

Table 3. EC: Voluntary Export Restraint Arrangements, March 1989

Major Known VERs (Excluding the MFA)	World- Wide	EC Total	EC- Wide	National <u>1/</u>	Restrained Exporters <u>2/</u>
Total	289	173	77	96	Benelux (13); Denmark (2); France (17); Greece (1); Germany (2); Ireland (2); Italy (17); Portugal (9); Spain (7); United Kingdom (26)
Steel	50	14	13	1	United Kingdom
Agricultural and food products	51	36	31	5	France (1); Ireland (1); Italy (2); Spain (1)
Automobiles and transport equipment	20	17	2	15	Belgium (1); France (2); Italy (3); Portugal (4); Spain (1); United Kingdom (4)
Textiles and clothing	66	27	24	3	Italy (1); Portugal (1); United Kingdom (1)
Electronic products	28	25	2	23	France (5); Germany (1); Italy (4); Portugal (1); Spain (1); United Kingdom (11)
Footwear	18	15	1 <u>4/</u>	14	Benelux (3); France (3); Ireland (1); Italy (3); United Kingdom (4)
Machine tools	14	4	1	3	France (1); Spain (1); United Kingdom (1)
Other	42	35	3	32	Benelux (9); Denmark (2); France (5); Greece (1); Germany (1); Italy (4); Portugal (3); Spain (3); United Kingdom (4)

Source: GATT, Review of Developments in the Trading System, March 1989.

1/ The September 1988-February 1989 GATT report on developments in the trading system indicates that 96 national VERs were in force as of March 1989, most of which are industry-to-industry arrangements. Of these, 26 VERs were reported for the United Kingdom. However, the U.K. authorities have indicated that they are aware of only eight such arrangements, which apply to imports of automobiles, transport equipment, and machine tools from Japan, as well as footwear from Czechoslovakia, Poland, and Romania. They have also indicated that two of these arrangements (forklift trucks and machine tools from Japan) were no longer justified and would be allowed to lapse.

2/ EC is the European Community; E. Eur. is East Europe; OLDCs are other developing countries; OICs are other industrial countries; LDCs are developing countries; ICs are industrial countries. The term "other" in OLDC and OIC refers to countries other than those identified in the particular classification.

3/ Not specified.

4/ Industry-to-industry arrangement.

Table 4. European Community:
Authorization of Article 115 $\frac{1}{2}$ Requests, 1980-91

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991 $\frac{1}{2}$	Total 1980- 1991
Belgium: Acceptances	25	17	19	22	14	4	0	1	2	0	0	0	104
Of which: agricultural products	18	16	17	16	12	2	0	1	2	0	0	0	87
As percent of requests	73	74	100	100	100	100	0	100	67	0	0	0	87
Denmark: Acceptances	4	0	0	0	0	0	0	2	0	0	0	0	6
Of which: agricultural products	4	0	0	0	0	0	0	2	0	0	0	0	6
Of which: textiles	0	0	0	0	0	0	0	0	0	0	0	0	0
As percent of requests	100	0	0	0	0	0	0	100	0	0	0	0	100
France: Acceptances	105	80	85	57	39	66	52	62	52	32	27	10	723
Of which: agricultural products	63	55	55	39	26	43	32	44	32	34	22	9	423
Of which: textiles	42	25	30	18	13	23	20	18	20	10	5	1	144
As percent of requests	84	73	76	59	66	80	78	86	87	83	80	91	79
Germany, Federal Republic of: Acceptances	1	2	2	4	0	0	0	0	0	0	0	0	9
Of which: agricultural products	1	2	2	4	0	0	0	0	0	0	0	0	9
Of which: textiles	0	0	0	0	0	0	0	0	0	0	0	0	0
As percent of requests	100	100	100	100	0	0	0	0	0	0	0	0	100
Greece: Acceptances	-	0	0	0	0	0	0	0	2	2	2	0	5
Of which: agricultural products	-	0	0	0	0	0	0	0	2	2	2	0	5
Of which: textiles	-	0	0	0	0	0	0	0	0	0	0	0	0
As percent of requests	-	0	0	0	0	0	0	0	100	100	100	0	100
Ireland: Acceptances	57	32	26	48	59	57	45	52	33	12	5	1	427
Of which: agricultural products	57	30	26	47	57	57	43	49	33	12	4	1	403
Of which: textiles	0	2	0	1	2	0	2	3	0	0	1	0	24
As percent of requests	49	56	79	91	84	89	68	87	87	71	80	20	72
Italy: Acceptances	23	23	29	37	34	30	20	23	19	17	18	14	287
Of which: agricultural products	14	11	14	19	11	7	3	8	8	10	10	10	109
Of which: textiles	9	12	15	18	23	23	17	15	11	7	8	4	178
As percent of requests	52	58	53	65	63	66	91	96	80	100	89	93	78
Portugal: Acceptances	-	-	-	-	-	-	0	1	1	1	1	1	5
Of which: agricultural products	-	-	-	-	-	-	0	1	1	1	1	1	5
Of which: textiles	-	-	-	-	-	-	0	0	0	0	0	0	0
As percent of requests	-	-	-	-	-	-	0	100	100	100	100	100	100
Spain: Acceptances	-	-	-	-	-	-	4	10	17	12	15	20	82
Of which: agricultural products	-	-	-	-	-	-	4	10	17	12	15	19	82
Of which: textiles	-	-	-	-	-	-	0	0	0	0	0	1	0
As percent of requests	-	-	-	-	-	-	100	77	74	36	43	43	62
United Kingdom: Acceptances	7	12	13	20	19	12	5	3	1	2	1	2	105
Of which: agricultural products	7	12	13	20	19	12	5	3	1	2	1	2	105
Of which: textiles	0	0	0	0	0	0	0	0	0	0	0	0	0
As percent of requests	23	50	65	95	76	76	83	60	100	100	100	100	78
Total EC acceptances	222	166	174	198	165	176	141	157	128	119	79	48	1763
Of which: agricultural products	164	120	114	131	120	119	102	105	76	78	48	32	1211
Of which: textiles	58	46	60	67	45	57	39	52	52	41	31	16	552
Other products	53	43	52	49	37	45	36	49	45	38	20	12	477
Rejected and withdrawn	134	89	67	65	50	35	43	25	25	42	28	33	667
Total requests	356	255	241	253	215	211	184	182	153	161	97	81	2430
Acceptances as percent of requests	62	65	72	74	77	83	197	86	84	74	71	59	74

Source: Data provided by the EC Commission.

Note: ... = not available; - = not applicable.

$\frac{1}{2}$ Temporary restrictions on free circulation of goods within the Community under Article 115 of the Treaty of Rome.

$\frac{2}{2}$ Only partially disaggregated data available for 1991.

Table 5. EC: Antidumping and Countervailing Investigations, 1983-88

	1983	1984	1985	1986	1987	1988
Investigations initiated	38	49	36	24	39 <u>1/</u>	40
By exporting country:						
Industrial countries	12	16	6	2	11 <u>1/</u>	7 <u>1/</u>
Of which: Japan	(4)	(4)	(2)	(1)	(7)	(4)
Developing countries	10	6	16	11	20	22
Of which: Korea	(--)	(--)	(1)	(1)	(5)	(7)
Centrally planned economies	16	27	14	11	8	11
Actions taken <u>2/</u>	69	43	21	35	29	46
Provisional duties	22	11	9	6	13	28
Definitive duties	20	5	8	4	9	18
Price undertakings	27	27	4	25	8	--

Sources: EC Commission documents (87)178, (89)106, and (90)229 Fourth, Sixth and Seventh Annual Report of the Commission on the Community's Antidumping and Antisubsidy Activities, Brussels, April 28, 1987, March 21, 1989, and June 13, 1990.

1/ The figures exclude seven investigations initiated under the EC "screwdriver" legislation to prevent circumvention of existing antidumping duties. These are listed separately on Table 6.

2/ Including actions on investigations initiated in previous years.

Table 6. European Community: Antidumping Investigations Under "Screwdriver" Legislation

Action	Product	Affected Exporter	Duty (per unit)	Date
Investigation initiated	Photocopiers	Japan		February 1988
Definitive duties	Photocopiers	Japan	ECU 28 to 225	October 1988
Duties revoked on basis of conformity to anti-dumping regulations	Photocopiers	Japan		February 1989
Investigation closed	Photocopiers--Ricoh brand	Japan	Negative finding	February 1990
Investigation initiated	Electronic scales	Japan		September 1987
Definitive duties	Electronic scales	Japan	ECU 22 to 66	April 1988
Duties revoked on basis of minimum price undertaking	Electronic scales	Japan		September 1988
Investigation initiated	Ball bearings	Japan		June 1988
Investigation closed	Ball bearings	Japan	Negative finding	January 1989
Investigation initiated	Electronic typewriters	Japan		September 1987
Definitive duties	Electronic typewriters	Japan	ECU 22 to 56	April 1988
Duties revoked on basis of minimum price undertaking	Electronic typewriters--Matsushita brand	Japan	ECU 41	May 1988
Duties revoked on basis of minimum price undertaking	Electronic typewriters	Japan		July 1988
Investigation initiated	Hydraulic excavators ^{1/}	Japan		June 1988
Investigation closed	Hydraulic excavators ^{1/}	Japan	Negative finding	August 1989
Investigation initiated	Earth-moving vehicles ^{1/}	Japan		June 1988
Complaint withdrawn	Earth-moving vehicles	Japan		February 1989
Investigation initiated	Dot matrix computer printers	Japan		December 1988
Definitive duties	Dot matrix computer printers	Japan		October 1989
Duties revoked on basis of minimum price undertaking	Dot matrix computer printers	Japan		November 1989
Investigation initiated	Video cassette records	Japan		July 1989

Sources: GATT, Review of Developments in the Trading System, (various issues); and European Report (various issues), and EC Commission.

^{1/} Initiated on the basis of Article 7 of Regulation EEC 2324/88.

Table 7. European Community: European Agricultural Guarantee and Guidance Fund--Guarantee Section, Expenditures by Sector, 1980-91

(In millions of ECUs)

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991 2/
Cereals 2/ and rice	1,714	1,943	1,875	2,534	1,698	2,360	3,485	4,237	4,337	3,340	3,950	5,477
Export subsidy	1,219	1,224	1,106	1,593	753	1,113	1,804	3,166	2,986	2,721	2,538	3,450
Intervention	509	719	769	941	945	1,247	1,681	1,071	1,351	619	1,412	2,027
Milk and products 2/ 3/	4,754	3,343	3,328	4,396	5,442	5,933	5,406	5,013	5,915	5,041	4,972	5,670
Export subsidy	2,746	1,896	1,521	1,327	1,943	2,028	2,155	2,258	3,014	2,922	1,947	2,732
Intervention	2,006	1,457	1,806	3,069	3,498	3,905	3,251	2,755	2,901	2,118	3,025	2,938
Oils and fats	687	1,025	1,214	1,621	1,752	1,803	2,632	3,827	3,917	4,138	4,647	6,041
Export subsidy	4	8	13	13	9	23	32	87	88	99	37	136
Intervention	683	1,017	1,201	1,608	1,743	1,780	2,600	3,740	3,829	4,039	4,510	5,905
Sugar 3/	567	768	1,242	1,316	1,632	1,805	1,726	2,035	2,082	1,980	1,391	1,948
Export subsidy	286	409	744	758	1,190	1,353	1,238	1,516	1,566	1,451	929	1,250
Intervention	289	358	498	558	442	452	487	519	516	529	462	698
Beef, veal, lamb, goat, pigmeat, and poultry	1,563	1,675	1,374	2,005	2,813	2,974	4,348	3,033	4,179	4,376	4,711	4,586
Export subsidy	893	1,042	844	1,072	1,620	1,504	1,387	1,142	1,135	1,776	1,535	1,660
Intervention	671	633	330	933	1,193	1,470	2,961	1,891	3,044	2,600	3,176	2,926
Fruits and vegetables	688	641	914	1,196	1,455	1,231	986	967	708	1,020	1,253	1,460
Export subsidy	41	43	60	58	59	75	77	67	65	80	81	119
Intervention	646	598	855	1,138	1,396	1,156	909	900	643	940	1,172	1,341
Other	1,023	1,508	2,146	2,363	3,204	3,411	3,014	3,150	4,365	4,189	4,012	5,354
All sectors	11,005	10,903	12,093	15,431	17,996	19,517	21,597	22,262	25,508	24,084	24,936	30,536
Accession compensatory amounts (ACAs)	--	--	--	--	--	--	6	18	64	42	37	35
Monetary compensatory amounts (MCAs)	298	238	313	488	376	190	476	636	505	272	195	156
All sectors, including ACAs and MCAs	11,314	11,141	12,406	15,920	18,372	19,707	22,079	22,919	26,073	24,397	25,167	30,727
Depreciation of intervention stocks	...	...	...	...	--	--	--	--	1,240	1,443	1,361	810
Other 4/	...	...	...	...	--	138	114	259	346	33	74	816
All sectors, including ACAs, MCAs, depreciation of intervention stocks and other	...	...	...	...	18,372	19,845	22,193	23,178	27,659	25,873	26,454	32,353

Sources: Commission of the European Communities, The Agricultural Situation in the Community (Brussels), various issues and Financial Report on the European Agricultural Guarantee and Guidance Fund.

1/ Preliminary draft budget.

2/ Including the financial contribution from cereal and milk producers.

3/ Including food aid refunds.

4/ Clearance of accounts plus interest following reform of financing arrangements, free distribution of intervention products and set-aside of arable land. Figure for 1987 includes clearance of the 1983, 1984 and 1985 accounts. Figure for 1990 also includes rural development schemes linked to market operation.

Table 8. European Community: Target Prices for Selected Commodities, 1980/81-1990/91 1/

	1980/81	1981/82	1982/83	1983/84	1984/85	1985/86	1986/87	1987/88	1988/89	1989/90 2/	1990/91 3/
Cereals (ECUs per ton)											
Common wheat	214.01	230.55	250.61	261.41	259.08	254.98	256.16	256.10	250.30	241.08	241.08
Barley	194.32	210.00	228.27	238.17	236.30	232.61	233.81	233.80	228.00	219.46	219.46
Rye	197.31	210.00	228.27	238.17	238.37	234.61	233.86	233.80	228.00	219.46	219.46
Rice, husked (ECUs per ton)											
	408.16	450.50	496.69	523.16	539.49	548.37	548.37	548.37	549.85	546.88	546.88
Sugar, white 4/ (ECUs per ton)											
	432.70	469.50	514.10	534.70	534.70	541.80	541.80	541.80	541.80	531.00	531.00
Olive oil (ECUs per ton)											
	2,479.70	2,727.70	3,027.70	3,194.20	3,162.30	3,225.60	3,225.60	3,225.60	3,225.60	3,225.60	3,225.60
Oilseeds (ECUs per ton)											
Sunflower	426.30	477.50	544.40	577.10	582.20	573.50	583.50	583.50	583.50	583.50	583.50
Colza and rapeseed	386.90	425.60	463.90	482.20	472.60	464.10	464.10	450.20	450.20	450.20	450.20
Wine, Type AII (ECUs per hectoliter)											
	55.69	61.26	68.00	71.74	71.02	71.02	71.02	69.60	69.60	69.60	69.60
Tobacco, #2 (ECUs per kilogram)											
	3.603	3.783	4.199	4.514	4.604	4.504	4.512	4.512	4.512	3.464	...
Fruits and vegetables (ECUs per 100 kilogram)											
Cauliflower	14.75	17.40	19.81	21.08	21.52	21.74	21.96	26.94	26.94	27.11	...
Tomatoes (open grown)	24.79	26.51/17.22	24.38/17.36	25.11/19.44	24.85/20.70	24.08/21.48	24.08/22.87	23.68	23.68	24.69	...
Oranges	32.14/19.38	35.53/26.28	38.27/30.87	40.75/35.49	40.97/38.32	39.74	39.74	38.74	38.74	35.62	...
Apples	20.42	22.54	28.49	29.49	29.63	29.63	29.63	29.63	29.63	28.06	...
Milk (3.7 percent fat content)											
	222.60	242.60	268.10	274.30	274.30	278.40	278.40	278.40	278.40	278.40	268.60
Beef animals (live)											
	1,607.60	1,728.20	1,918.70	2,070.90	2,050.20	2,050.20	2,050.20	2,050.20	2,050.20	2,050.20	2,000.00
Pork											
	1,587.21	1,761.80	1,946.80	2,053.90	2,033.30	2,033.30	2,033.30	2,033.30	2,033.30	2,033.30	1,900.00
Sheep and goat meat (ECUs per 100 kilogram)											
	345.00	370.88	409.82	432.36	428.04	432.32	432.32	432.32	432.32	432.32	432.32

Sources: Commission of the European Communities, The Agricultural Situation in the Community (Brussels), various issues, and Bulletin of the European Communities (Brussels), various issues.

1/ Beginning of marketing year.

2/ Prices for cereals, rice and sugar include the application of the stabilizer system (Regulation 1412/89). For milk, price also includes the reduction decided upon as part of the increase in the milk quota of 1 percent.

3/ Prices for cereals, rice and sugar exclude the application of the stabilizer system.

4/ Intervention price.

5/ Sheep meat and goat meat were not covered by the Common Agricultural Policy prior to 1980/81.

Table 9. European Community: Average Increase in Common Agricultural Prices, 1985/86-1990/91

(In percent)

	1986/87			1987/88			1988/89			1989/90			1990/91		
	Common Prices in			Common Prices in			Common Prices in			Common Prices in			Common Prices in		
	National	Inflation		National	Inflation		National	Inflation		National	Inflation		National	Inflation	
	ECUs 1/	currency 2/	1986 3/	ECUs 1/	currency 2/	1987 3/	ECUs 1/	currency 2/	1988 3/	ECUs 1/	currency 2/	1989 3/	ECUs 1/	currency 2/	1990 3/
Germany, Fed.															
Rep. of	-0.2	-0.2	3.3	--	--	1.9	--	--	1.5	-0.1	-0.8	2.6	-1.5	-1.9	3.4
France	-0.3	2.0	5.2	-0.2	4.1	3.0	--	1.1	2.9	-0.2	1.0	3.2	-0.7	0.7	2.8
Italy	-0.6	4.2	7.9	-0.6	3.3	6.0	-0.3	1.9	6.6	-0.7	0.9	6.0	-1.3	-1.0	7.5
Netherlands	--	--	0.4	--	-0.5	-0.6	--	-0.2	1.6	-0.1	-0.6	1.6	-1.9	-1.9	2.9
Belgium	-0.1	1.7	3.7	--	1.7	2.2	--	0.4	1.6	-0.1	-0.1	4.5	-1.9	-1.9	3.1
Luxembourg	-0.1	1.7	--	--	1.6	--	--	0.4	--	--	--	--	-0.6	-0.6	--
United Kingdom	-0.5	1.9	3.5	--	6.3	5.0	--	2.4	5.5	-0.1	3.0	7.1	-0.8	7.5	6.4
Ireland	-0.3	2.5	6.3	--	8.5	2.5	--	0.9	3.2	--	1.6	5.2	-0.4	0.7	3.2
Denmark	-0.7	1.2	4.7	--	2.3	5.0	--	0.7	4.0	-0.1	0.6	3.8	-2.3	-2.3	3.1
Greece 4/	-0.5	13.5	17.4	-0.4	13.3	13.8	-0.6	14.2	15.8	-0.5	14.1	14.1	-1.0	2.5	20.0
Spain 5/	1.8	3.3	11.9	1.8	7.2	5.8	1.3	1.1	5.6	1.4	-0.2	7.0	-0.4	0.6	7.3
Portugal 5/	0.3	1.7	20.5	0.5	6.1	11.3	0.7	8.5	11.5	6.7	9.0	13.2	0.7	0.7	14.0
Average 6/	-0.3	2.2	5.2	-0.2	3.3	3.7	--	1.6	4.1	-0.1	1.2	4.6	-1.1	0.3	5.0

Sources: Commission of the European Communities, The Agricultural Situation in the Community (Brussels), various issues.

- 1/ Common price in European currency units (ECUs) (intervention price or equivalent price) weighted by national agricultural production.
2/ Common price in ECUs converted into national currency at "green" exchange rate, after adjustment in "green" rate by all measures taken.
3/ Rate of inflation measured by the GDP deflator (agricultural year) prior to 1986; from 1986, calendar-year basis.
4/ Including adjustments of Greek prices resulting from membership agreements.
5/ Including the impact of the alignment on common prices according to the accession agreements from 1987/88 on.
6/ These figures refer to the average of EC(10) for 1985/86, 1986/87 and 1987/89.

Table 10. EC, Japan, United States: Producer Subsidy Equivalent (PSEs)

	1978-85	1985	1986	1987	1988	1989	1990	1991
<u>PSEs</u>								
(In percent of producer prices)								
EC <u>2/</u>	35	43	50	49	46	41	49	49
Japan	64	69	75	76	74	70	66	66
United States	26	32	42	40	34	28	29	30
<u>PSEs per farmer</u>								
(In thousands of U.S. dollars per farmer)								
EC <u>2/</u>	7	8	8	10	10	9	13	13
Japan	8	9	14	16	18	17	16	17
United States	14	18	26	26	23	19	22	22
<u>PSEs per hectare</u>								
(In U.S. dollars per hectare)								
EC <u>2/</u>	412	478	590	674	651	574	810	784
Japan	5,079	5,641	8,690	9,089	9,543	8,766	7,981	8,422
United States	79	97	126	128	107	91	99	98

Source: OECD Agricultural Policies, Markets and Trade: Monitoring and Outlook, Paris (1989, 1990, 1991, 1992 issues).

1/ Estimates.

2/ EC(10) in 1979-85; EC(12) in 1986-89.

Table 11. EC: Total Volume of State Aids and National Aids by Sector and Function

(Average, 1988-90 in 1989 prices)

	Bel- gium	Den- mark	Ger- <u>1</u> / many	Greece <u>2</u> / Greece	France	Ireland	Italy	Luxem- bourg	Nether- lands	Port- ugal	Spain	United Kingdom	EC(12)
Total volume of state aid													
In billion ECU	3.8	1.1	25.8	1.5	16.0	0.6	22.7	0.3	2.6	0.9	6.0	8.2	89.5
In ECU per person employed	1,040	409	971	387	735	564	982	1,389	528	245	480	312	687
In percent of GDP	2.8	1.1	2.4	3.1	1.8	2.0	2.9	4.0	1.3	2.2	1.8	1.1	2.0
	(In percent of total state aid)												
State aid by sector/function	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.00	100.00	100.0	100.0
Industry/services	87.5	71.8	70.4	75.0	82.5	54.9	57.7	81.3	73.0	76.5	93.8	77.2	72.4
Horizontal objectives <u>3</u> / Sector-specific	23.9	18.4	8.7	58.5	25.2	29.7	14.5	7.5	36.7	11.7	11.6	17.5	16.7
Steel	63.6	53.4	61.7	16.5	57.3	25.2	43.2	73.8	36.3	64.8	82.2	59.7	55.7
Coal <u>4</u> / Shipbuilding	0	0	0.2	0.1	0.1	0	3.0	0	0	15.9	12.1	0	1.8
Transport <u>4</u> / Other sectors	27.8	0	32.4	0	17.0	0	0	0	0	0.4	19.4	41.8	18.7
	0.4	10.0	0.9	2.3	1.6	0	1.8	0	3.4	18.5	4.2	2.9	2.0
	34.7	41.6	26.0	13.2	30.7	19.9	36.0	73.7	31.2	11.4	34.8	10.1	29.0
	0.7	1.8	2.2	0.9	7.9	5.3	2.4	0.1	1.7	18.6	11.7	4.9	4.2
Regional aid	6.5	1.1	18.5	10.7	3.3	24.9	26.9	11.6	5.8	3.6	2.1	13.1	15.0
Agriculture and fisheries <u>4</u> / 	6.0	27.1	11.1	14.2	14.2	20.2	15.4	7.2	21.2	19.9	4.1	9.7	12.6

Source: EC Commission, "Second Survey of State Aids in the European Community," 1990; adapted from Tables XI, XII and Annex IV.

1/ Excludes aid to former German Democratic Republic.2/ Tentative.3/ Includes state aids for innovation and research and development, environment, small and medium-sized firms, energy-saving investment, and other nonsector-specific objectives.4/ State aids provided principally under EEC Treaty regulations.

Table 12. EC: Degree of Subsidization in Selected Sectors

(In percent of gross sectoral value added; 1988-90)

	Belgium	Denmark	Germany <u>1/</u>	Greece <u>2/</u>	France	Ireland	Italy	Luxem- bourg	Nether- lands	Portugal	Spain	U.K.	EC(12)
Total state aid <u>3/</u>	2.8	1.1	2.4	3.1	1.8	2.0	2.9	4.0	1.3	2.2	1.8	1.1	2.0
Manufacturing	4.1	2.1	2.5	14.6	3.5	4.9	6.0	2.6	3.1	5.3	3.6	2.0	3.5
Of which:													
Shipbuilding	14.5	66.4	25.1	13.0	55.0	...	84.8	...	23.4	78.6	34.1	10.8	34.3
Agriculture <u>4/</u>	8.5	8.1	20.0 <u>2/</u>	3.2	9.0	4.4	12.9	15.5 <u>8/</u>	6.4 <u>8/</u>	10.1	1.3	8.6	9.6
Railways <u>5/</u>	54.8	14.8	28.7	6.4	25.2	14.6	6.9	160.1	5.7	8.4	26.3	5.9	12.4
Coal mining <u>6/</u>	252,412	...	60,219	...	108,349	...	...	...	...	4,117	27,517	40,071	...

Source: EC Commission, "Third Survey of State Aids in the European Community," 1990, Tables I, III, IV, V, VI and XII.

1/ Excludes aid to former German Democratic Republic.2/ Data are tentative.3/ In percent of GDP.4/ Through national state aids only; support through the EC budget is additional. The figures for Germany include aid given by way of VAT advantages.5/ Railways and inland waterways. Aid figures for Greece, Ireland, and the Netherlands are expressed as a percentage of value-added in whole transport sector.6/ Aid to coal mining as ECU per employee in coal mining; value-added figures are not available.7/ Includes aid from VAT advantages.8/ Based on national accounts data or long-term extrapolations; not comparable with figures for other member states. These estimates have nevertheless been included in the total aid figures.

Table 13. EC: National State Aids by Type 1/

(In percent of total state aid; average, 1988-90)

	Belgium	Denmark	Germany	Greece <u>2/</u>	France	Ireland	Italy	Luxem- bourg	Nether- lands	Portugal	Spain	U.K.	EC(12)
Grants	85.7	87.3	78.1	59.0	72.6	70.2	77.0	96.3	83.8	54.7	90.9	91.6	79.0
Tax reductions	8.6	1.1	18.5	12.2	5.9	26.2	19.5	0.0	12.8	2.0	0.0	1.6	12.6
Equity participation	1.5	0.0	0.0	12.7	4.3	1.5	2.4	0.0	0.0	40.2	4.1	2.9	2.6
Soft loans	1.6	11.5	2.0	7.7	5.5	0.0	1.2	3.1	2.1	2.5	4.6	1.1	2.6
Tax deferrals	0.0	0.0	1.0	0.0	1.1	0.0	0.0	0.0	0.0	0.0	0.0	2.3	0.8
Guarantees	2.6	0.0	0.0	8.3	10.6	2.1	0.0	0.6	1.3	0.6	0.0	0.5	2.4

Source: EC Commission, "Third Survey of State Aids in the European Community," 1992; Annex IV.

1/ The data includes only the estimated aid component of state aids, i.e., figures on equity participation include only the portion needed to cover recurrent operating deficits, soft loans include only the grant element of the loan, tax deferrals the present discounted value of the benefit to the recipient, and guarantees are included only if exercised.

2/ Data for Greece are tentative.

References

- Abrams, R.K. et al., *The Impact of the EC's Internal Market Nonmember Countries: The Case of EFTA*, IMF Occasional Paper No. 74 (Washington: International Monetary Fund, December 1990).
- Brada, Josef C., *Regional Integration in Eastern Europe* (World Bank and CEPR, April 1992).
- Canada, Bureau of Competition Policy, *Canadian Competition Policy: Its Interface with Other Economic and Social Policies, A Framework for Discussion* (Ottawa: Bureau of Competition Policy, Consumer and Corporate Affairs, September 1989).
- Centre for Economic Policy Research, *Developments in Eastern Europe: Their Impact on Western Europe* (London, November 1990).
- Commission of the European Communities, "Single European Act," *Bulletin of the European Communities*, Supplement 2/86 (1984), Luxembourg, and various issues of the Bulletin.
- _____, *Completing the Internal Market*, White Paper from the Commission to the European Council, COM(85)310 (Brussels, June 1985).
- _____, "The Economics of 1992," *European Economy*, No. 35 (March 1988).
- _____ (1989a), *Eighteenth Report on Competition Policy*, Brussels. Also past reports.
- _____ (1989b), "The Community Economy at the Turn of the Decade," *European Economy*, No. 42, Special Edition, October.
- _____ (1990a), *The Agricultural Situation in the Community*; 1989 Report, Brussels. Also past reports.
- _____ (1990b), *Seventh Annual Report of the Commission on the Community's Antidumping and Antisubsidy Activities*, COM(90)229, Brussels, June; and previous reports.
- _____ (1988, 1990c, 1992), *Survey of State Aids in the European Community*, Brussels.
- _____ (1990d), *Fifth Report of the Commission to the Council and the European Parliament Concerning the Implementation of the White Paper on the Completion of the Internal Market*, COM(90)90, Brussels, March.

_____, *Official Journal*, various issues.

de la Torre, Augusto, and Margaret R. Kelly, *Regional Trade Arrangements*, IMF Occasional Paper No. 93 (Washington: International Monetary Fund, February 1992).

Delors Committee, *Report on Economic and Monetary Union in the European Community*, Committee for the Study of Economic and Monetary Union (1989).

de Melo, J. and P. Messerlin, "Effects of European VERs on Japanese Autos," *European Economic Review*, Vol. 32 (September 1988), pp. 1527-46.

European Report, Brussels, various issues.

Finger, J.M., Hall, H.K. and Nelson, R., "The Political Economy of Administered Protection," *American Economic Review*, Vol. 72 (June 1982), pp. 452-66.

Finger, J.M., *GATT's Influence on Regional Arrangements*, World Bank and CEPR papers (April 1992).

General Agreement on Tariffs and Trade, *Review of Developments in the Trading System*, Geneva, various issues.

_____, *GATT Focus*, various issues.

_____, *Uruguay Round News*, various issues.

_____, *European Communities 1991*, Trade Policy Review Series, Geneva.

Giersch, H., "EC 1992: Prospects and Problems," Paper presented at the McGill Economic Center Conference, Toronto (May 1989).

Hindley, B., "Dumping and the Far-East Trade of the European Community," *The World Economy*, Vol. II, No. 4 (December 1988).

Hoeller, Peter and Markku Wallin, "Energy Prices, Taxes and Carbon Dioxide Emissions", *OECD Economic Studies*, No. 17 (Autumn 1991).

Hufbauer, Gary Clyde, *Europe 1992: An American Perspective*, (Washington: Brookings Institution, 1990).

Jackson, J.H., *World Trade and the Law of GATT*, Bobbs-Merrill (1969).

Julius, deAnne, *Foreign Direct Investment: the Neglected Twin of Trade*, IMF Occasional Paper No. 33 (Washington: Group of Thirty, 1991).

- Kelly, M. et al., *Issues and Developments in International Trade Policy*, IMF Occasional Paper No. 63 (Washington: International Monetary Fund, December 1988).
- _____, *Issues, Developments in International Trade Policy*, IMF World Economic and Financial Surveys (August 1992).
- Kopits, George (ed.), *Tax Harmonization in the European Community*. IMF Occasional Paper No. 94 (Washington: International Monetary Fund, July 1992).
- Lipschitz, L. et al., *The Federal Republic of Germany - Adjustment in a Surplus Country*, IMF Occasional Paper No. 64 (Washington: International Monetary Fund, January 1989).
- Mundell, R.A., "The Theory of Optimum Currency Areas," *American Economic Review*, Vol. 51, pp. 657-64 (September 1961).
- Organization for Economic Cooperation and Development, *Structural Adjustment and Economic Performance* (Paris: OECD, 1987).
- _____, *Agricultural Policies, Markets and Trade: Monitoring and Outlook* (Paris: OECD, 1990, 1991, 1992).
- Pohl, Gerhard and Piritta Sorsa, *European Integration and Trade with Developing Countries*, World Bank Policy and Research Series (forthcoming, 1992).
- Rosenblatt, J. et al., *The Common Agricultural Policy of the European Community: Principles and Consequences*, IMF Occasional Paper No. 62 (Washington: International Monetary Fund, November 1988).
- The Economist Intelligence Unit, *European Trends*, various issues. United States Government Task Force on the EC Internal Market, *EC 1992: An Assessment of Economic Policy Issues Raised by the European Community's Single Market Program* (Washington, May 1990).
- Trade and Competition Policy: The Consumer Interest*, International Trade and the Consumer, National Consumer Council, Working Paper No. 5 (London: National Consumer Council, March 1991).
- Ungerer, et al., *European Monetary System, Developments and Perspectives*, IMF Occasional Paper No. 73 (Washington: International Monetary Fund, 1990).
- Winters, Alan, *The European Community: A Case of Successful Integration?*, World Bank and CEPR Papers (April 1992).
- Wolf, M., "The Dumping Inquisition," *Financial Times* (August 1988).