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Summary record of the 1494th meeting

Topic:
Most-favoured-nation clause

Extract from the Yearbook of the International Law Commission:-
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1494th MEETING

Tuesday, 6 June 1978, at 10.05 a.m.

Chairman: Mr. José SETTE CÂMARA

Members present: Mr. Calle y Calle, Mr. Dadzie, Mr. Díaz González, Mr. El-Erian, Mr. Francis, Mr. Jagota, Mr. Njenga, Mr. Quentin-Baxter, Mr. Reuter, Mr. Riphagen, Mr. Šahović, Mr. Schwebel, Mr. Sucharitkul, Mr. Tabibi, Mr. Tsuruoka, Mr. Ushakov, Sir Francis Vallat, Mr. Verosta.

The most-favoured-nation clause (*continued*) (A/CN.4/308 and Add.1 and Add.1/Corr.1, A/CN.4/309 and Add.1 and 2)

[Item 1 of the agenda]

DRAFT ARTICLES ADOPTED BY THE COMMISSION: SECOND READING (*continued*)

ARTICLE 21 (The most-favoured-nation clause in relation to treatment under a generalized system of preferences)

1. The CHAIRMAN invited the Special Rapporteur to introduce article 21, which read:

Article 21. The most-favoured-nation clause in relation to treatment under a generalized system of preferences

A beneficiary State is not entitled under a most-favoured-nation clause to any treatment extended by a developed granting State to a developing third State on a non-reciprocal basis, within a generalized system of preferences established by that granting State.

2. Mr. USHAKOV (Special Rapporteur) said that, with article 21, the Commission was entering the sphere of general exceptions of the operation of the most-favoured-nation clause. That article, designed to meet the needs of developing countries, was based on the generalized system of preferences (GSP) established by UNCTAD and GATT, which was generally accepted by the international community of States. As the Commission had stressed in its commentary, the system was "non-reciprocal and non-discriminatory";[1] it laid down primary rules for relations between developed and developing countries, which were generally applied in the activities of United Nations bodies.

3. He drew the Commission's attention to the "agreed conclusions" reached by the Special Committee on Preferences set up by resolution 21 (II) of the United Nations Conference on Trade and Development as a subsidiary organ of the Trade and Development Board; experts from those conclusions, which were annexed to decision 75 (S-IV) adopted by the Board at its fourth special session, were reproduced in the Commission's commentary.[2] He referred, in particular, to section III (Safeguard mechanisms), which stated that

> The preference-giving countries reserve the right to make changes in the detailed application as in the scope of their measures, and in particular, if deemed necessary, to limit or withdraw entirely or partly some of the tariff advantages granted.

Developed countries were thus entirely free to limit or even to withdraw completely the advantages granted to developing countries under the GSP established for their benefit.

4. He also drew attention to section IV (Beneficiaries) of the "agreed conclusions", in which the Special Committee noted that, "as for beneficiaries, donor countries would in general base themselves on the principle of self-election". Thus donor countries were entirely free to choose the countries that would benefit from the generalized system of preferences.

5. According to the conclusion in section VI (Duration) of the same document, the initial duration of the GSP had been set at 10 years. The Commission had thus endeavoured to promote the progressive development of existing law by adopting a general rule on a system that had been set up on a merely provisional basis. But it had recognized that "the usefulness of article 21 depends upon the permanence and the development of the generalized system of preferences".[3] In that connexion, he stressed that the Commission was not called upon to ensure the permanence of the GSP; that was a matter for the States that had adopted the system.

6. In section IX of its conclusions (Legal status), the Special Committee on Preferences had recognized that

> no country intends to invoke its right to most-favoured-nation treatment with a view to obtaining, in whole or in part, the preferential treatment granted to developing counries in accordance with Conference resolution 21 (II) [of UNCTAD]...

7. The Commission had endorsed that conclusion and had noted that

> There seems to be general agreement... that States will refrain from invoking their rights to most-favoured-nation treatment with a view to obtaining in whole or in part the preferential treatment granted to developing countries by developed countries.[4]

It had thus established, as a general rule, an exception in favour of the GSP, so that the functioning of that system should not be hampered by the operation of the most-favoured-nation clause.

8. He noted that the Commission had stated in its commentary that

> The rule contained in article 21 applies to any State beneficiary of a most-favoured-nation clause irrespective of whether it belongs to the developed or to the developing category.[5]

The GSP was established by the granting State, which was therefore entirely free to decide not only what preferences it would grant to developing countries, but also which developing countries would ben-

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[1] *Yearbook... 1976*, vol. II (Part Two), p. 58, doc. A/31/10, chap. II, sect. C, art. 21, para. (3) of the commentary.

[2] *Ibid.*, pp. 59-60, para. (5) of the commentary.

[3] *Ibid.*, p. 63, para. (14) of the commentary.

[4] *Ibid.*, para. (13) of the commentary.

[5] *Ibid.*, para. (19) of the commentary.

efit from them. Thus the notion of a developing State varied from one granting State to another. Generally speaking, the political conception of a developing State, which was generally recognized by the international community and corresponded to the enlarged Group of 77, did not apply to economic and trade relations, for developing States were at very different levels of economic development. Unlike the political conception, the economic conception of a developing State was thus extremely variable and it was for each granting State to define what it meant by a "developing State" in the context of the GSP.

9. For example, under the GSP established by Hungary, to which the Commission had referred in its commentary,

> beneficiary countries are those developing countries in Asia, Africa and Latin America whose *per capita* national income is less than Hungary's.[6]

According to that definition, a country whose *per capita* income was greater than Hungary's was not, for Hungary, a developing country, although it might be regarded as such by antoher country for the purpose of the GSP. To that first condition Hungary had added three others: it considered that beneficiary countries were countries

> which do not apply discrimination against Hungary; which maintain normal trade relations with Hungary and can give reliable evidence of the origin of products eligible for preferential tariff treatment.[6]

10. It thus appeared that, if the Commission tried to lay down a general rule for developed and developing countries, it would be very difficult to interpret the principle of freedom of choice by the granting State, on which the GSP was based. In any event, it was virtually impossible to give a general definition of developing and developed States in the context of international economic and trade relations. In that connexion, he pointed out that the Commission

> took cognizance of the fact that there is at present no general agreement among States concerning the concepts of developed and developing States.[7]

However, the problem of the definition of those concepts did not arise in article 21, since it was the granting State itself that drew up the list of developing countries to which it decided to grant preferences under the GSP. Moreover, the Commission had stressed that "the system is based on the principle of self-selection, i.e. that the donor countries have the right to select the beneficiaries of their system and withhold preferences from certain developing countries,[8] and had also taken "account of the fact that the countries establishing their own preferential system were free to withdraw their grants in whole or in part".[9]

11. With the exception of the comment by Sweden to the effect that, in view of the temporary nature of generalized systems of preferences, it was not desirable "to grant to those systems a special legal status by including a specific article on those preferences in the draft articles regarding the most-favoured-nation clause" (A/CN.4/308 and Add.1 and Add.1/Corr.1, sect. A), most of the written and oral comments by governments and organizations favoured the retention of article 21 and related not so much to the article itself as to the inclusion in the draft of new provisions making exceptions in favour of developing countries.

12. In reply to the oral comments of certain representatives in the Sixth Committee who had considered that "it was not quite clear how generalized the system of preferences hould be in order to qualify for the exception provided in article 21" (see A/CN.4/309 and Add.1 and 2, para. 258), he said that it was not for the Commission but for States to generalize the system of preferences.

13. In his opinion, the suggestion of the Government of Colombia that the word "developed" should be inserted before the words "beneficiary State" in order to prevent the most-favoured-nation clause from creating "an imbalance in international trade and [giving] rise to inequitable and non-reciprocal benefits" (A/CN.4/308 and Add.1 and Add.1/Corr.1, sect. A), was contrary to the principle of self-selection by the granting State on which the GSP was based. Indeed, as the Commission had pointed out in its commentary,

> The provision must apply also to developing beneficiary States because if it did not the basic principle of the generalized system of preferences—the principle of self-selection—could be circumvented.[10]

14. There had been three main proposals relating to the inclusion in the draft articles of new provisions making exceptions to the most-favoured-nation clause in favour of developing countries: the first, made by EEC (A/CN.4/308 and Add.1 and Add.1/Corr.1, sect. C, 6, para. 6) and supported by the Netherlands (*ibid.*, sect. A), sought to enlarge the scope of article 21 by referring in it not only to the GSP but also to the special links resulting from preferential agreements concluded by industrialized States with developing countries; the second, made by the United States (*ibid.*), sought to include in article 21 a provision similar to the GATT missions that afforded some protection to third States benefiting under a most-favoured-nation clause; the third, made by ECWA (*ibid.*, sect. B) and supported by the German Democratic Republic (*ibid.*, sect. A), related to the preferences and advantages that developing countries granted to each other in their mutual relations.

15. With regard to the first proposal, the secretariat of GATT had indicated in its comments (*ibid.*, sect. C, 3) that a group set up by the Trade Negotiations Committee was in process of developing the "legal framework" for a differential system of pref-

[6] *Ibid.*, p. 61, para. (9) of the commentary.

[7] *Ibid.*, p. 63, para. (19) of the commentary.

[8] *Ibid.*, para. (17) of the commentary.

[9] *Ibid.*, para. (15) of the commentary.

[10] *Ibid.*, para. (19) of the commentary.

erences, similar to the GSP, that would provide differential and more favourable treatment for developing countries in relation to the provision of the General Agreement on Tariffs and Trade. The treatment that would be accorded to developing countries under that system on a non-reciprocal basis would constitute an exception to the application of the most-favoured-nation clause.

16. If that system of differential treatment were already well established and generally recognized, as was the GSP, he would be quite willing to mention it in article 21 along with the GSP or to devote a separate article to it. But as the system was still being worked out and its legal effect had not yet been defined, it would be difficult to refer to it in the draft articles. The term "preferential régime" used the amendment proposed by EEC did not seem clear. Nevertheless, if the Commission could define the notion of a preferential régime and considered that such a notion was generally recognized, the scope of article 21 could be widened on the basis of the text proposed by EEC.

17. With regard to the United States proposal, he thought it would be difficult to include in article 21 the system of protection provided for by GATT, because that system was not generally recognized and its inclusion would be contrary to the principle of self-selection on which the GSP was based.

18. As to the ECWA proposal for the exclusion from the application of the most-favoured-nation clause of the preference and advantages granted by developing countries to each other in their mutual relations, he fully supported the view that developing countries were under no obligation to extend to developed countries, in particular under a most-favoured-nation clause, the preferences and advantages they granted to each other to promote their economic development. However, under the ECWA proposal, no beneficiary State, even if it were a developing State, would be entitled by virtue of the most-favoured-nation clause to any treatment extended by a developing granting State to a developing third State in the context of preferential trade agreements. He would therefore suggest that the word "developed" should be inserted before the words "beneficiary country" in the text of that proposal, so as to reflect the idea expressed in article 21 of the Charter of Economic Rights and Duties of States,[11] that, in order to promote the expansion of their mutual trade, developing countries could "grant trade preferences to other developing countries without being obliged to extend such preferences to developed countries". There again, however, the problem arose of what was meant by a "developed State" and a "developing State" in the context of international trade relations. He was nevertheless prepared to try to take the ECWA proposal into account, although he foresaw that it would give rise to difficulties.

19. Mr. NJENGA pointed out that, as noted in the UNCTAD memorandum quoted in paragraph (3) of the commentary, the generalized non-reciprocal, non-discriminatory system of preferences for the benefit of developing countries had three objectives: to increase the increase the export earnings of the developing countries, to promote their industrialization and to accelerate their rates of economic growth. Consequently, it was necessary at that juncture to examine the extent to which the system met those objectives and to determine whether the draft would prove generally acceptable as the basis for a future convention. In his oral presentation, the Special Rapporteur had given a clear idea of the functioning of the system and of its inbuilt weaknesses.

20. In its "agreed conclusions" (excerpts from which were reproduced in paragraph (5) of the commentary), referring to the legal status of the system, the Special Committee on Preferences, established under UNCTAD resolution 21 (II), had taken note of the statement by the preference-giving countries that the system would be governed by the consideration that the tariff preferences were temporary in nature, that their grant did not constitute a binding commitment and, in particular, that it would in no way prevent their subsequent withdrawal in whole or in part or the subsequent reduction of tariffs on a most-favoured-nation basis, whether unilaterally or following international tariff accommodations. Moreover, the grant of tariff preferences would be conditional on the necessary waiver or waivers in respect of existing international obligations, in particular of those arising from the General Agreement on Tariffs and Trade. Thus it was possible to identify a number of serious shortcoming in the system.

21. Admittedly, the system might be continued beyond the initial period of 10 years, but it was essentially a stopgap measure and it would not resolve the long-term problem. Moreover, despite the existence of the system, the current economic situation was in many respects worse than that prevailing at the time of the first session of UNCTAD, in 1964. Other measures were therefore required if the current trend were to be reversed. Tariff preferences were wholly at the discretion of the donor country, since they could be withdrawn at any time, and the system could also be gravely undermined by subsequent reductions of tariffs granted on a most-favoured-nation basis.

22. It should also be noted that the principle of selection of beneficiaries by the donor country was in effect contrary to the original purpose of the scheme, which had been to create a non-discriminatory system. If the donor could select the beneficiary in the light of economic or even political considerations, the system might easily lead to discrimination between developing countries, as had indeed happened in the past. (For example, before the conclusion of the Lomé Convention,[12] a serious criticism of the

[11] General Assembly resolution 3281 (XXIX).

[12] Convention between the European Economic Community and 46 African, Caribbean and Pacific States.

Yaoundé Convention[13] had been that it tended to favour a particular group, namely, the former French colonies.) In addition, by virtue of the principle of self-selection, donor countries were entitled to choose not only the beneficiaries but also the products to be covered by the preferences, and they sometimes excluded or set strict limits on imports of the very items in which developing countries held a competitive position, for example, textiles and shoes in the case of the EEC scheme of generalized preferences.

23. Another disadvantage of the GSP was that it applied only to manufactures and semi-manufactures. Paragraph (11) of the commentary pointed out that, according to the report of the Trade and Development Board on its fifth special session, representatives of developing countries had judged that the system was of little or no benefit, since their countries did not produce manufactures or semi-manufactures, but supplied only primary materials and semi-processed agricultural commodities that were not covered by the system. That was clearly a major drawback for developing countries, particularly the countries of Africa and the smaller countries of Asia and Latin America. At the same session of the Board, representatives of developing countries had also observed that the actual benefits of the scheme were still meagre because of the limited coverage, the limitations imposed on preferential imports by ceilings and the application of non-tariff barriers to the products covered.

24. In that connexion, it was essential to take account of the effects of economic unions such as EEC, which were designed to set up a wall against non-members. However, there was a major difference between economic unions of developed countries and those of developing countries. The purpose of economic unions of developing countries was to facilitate development, whereas that of economic unions of developed countries was to expand their markets and to compete with other blocs of developed countries. The barrier thus erected against non-member countries could be lowered to some extent, but it would not be removed, especially in the case of sensitive products. Last, but by no means least, there were the many kinds of non-tariff barriers, which were often more prejudicial than the tariff barriers themselves.

25. He fully endorsed article 21 in its existing form, but thought it should be supplemented by a new article 21 *bis*, which would read:

With a view to promoting the expansion of their mutual trade, developing countries may grant trade preferences to other developing countries in accordance with bilateral or regional arrangements, without being obliged to extend such preferences to developed countries on the basis of the most-favoured-nation clause. Such arrangements shall not constitute an impediment to general trade libieralization and expansion.[14]

That formulation was an improvement on the ECWA proposal, as it did not create a situation of discrimination between developing countries. Many developing countries had emphasized the need to expand trade among themselves, and it was essential to do so outside the overall system created by GATT. Article 21 *bis* was simply a further incentive to help developing countries to arrive at a situation in which they would be able to compete with other States on a non-discriminatory basis. If the article were seen as an element in the progressive development of international law, it would be wholly justifiable for the Commission to take account of existing economic realities.

26. Mr. REUTER said it was his understanding that article 21 *bis* did not establish an obligation to grant advantages under a most-favoured-nation clause to developed countries, but that it established an obligation to grant such advantages to developing countries. Consequently, if a Latin American economic union abolished customs duties on certain products as among its members and a member of that union concluded a treaty containing a most-favoured-nation clause with Hong Kong, the economic union would have to extend to Hong Kong the benefit of that clause.

27. Mr. CALLE y CALLE said that article 21 provided for the first of the exceptions to the application of the most-favoured-nation clause. It dealt with an express exception, embodied in the clause itself, and had been introduced because the Commission shared the concern of mankind at the flagrant imbalance between the economies of countries at differing levels of development. That was a major problem and had given rise to new principles as well as to recognition of the fact that equal treatment of unequal subjects could lead to injustice.

28. In its commentary to article 21, the Commission had first noted General Principle Eight of recommendation A.I.1 adopted by UNCTAD at its first session. According to the secretariat of UNCTAD, it followed from that principle that the application of the most-favoured-nation clause to all countries, regardless of their level of development, would satisfy the conditions of formal equality, but would in fact involve implicit discrimination against the weaker members of the international community. Under the terms of General Principle Eight, developing countries need not extend to developed countries preferential treatment in operation among themselves. Developed countries, for their part, were to grant concessions to all developing countries and extend to those countries all the concesssions they granted to one another, without requiring reciprocity.[15]

29. Article 21 was based on the principle of equity, which had received wide support in the Sixth Committee of the General Assembly. Various positions had been adopted on the article. Some representa-

[13] Convention of Association between the European Economic Community and the African and Malagasy States associated with that Community.

[14] Subsequently circulated as document A/CN.4/L.266.

[15] See *Yearbook... 1976*, vol. II (Part Two), p. 8, doc. A/31/10, para. 42.

tives had held that it should be retained as it stood, since it represented the most that could be done for the developing countries. That view was shared by the Special Rapporteur, who had concluded in his report, after considering various proposals for the addition of new provisions, that it would not be advisable to change the terms of the article (A/CN.4/309 and Add.1 and 2, para. 281). Other representatives had held that article 21 should not be confined to trade matters, but should be extended to cover all systems of preferential treatment. They had maintained that there was a wide range of subjects for international co-operation, including financial assistance and the transfer of technology, that could be covered by an article of wider scope. In that connexion it had been observed that, logically, the order of the exceptions to the application of the clause should be changed so as to proceed from the general to the particular. The latter exceptions would cover such matters as frontier traffic, facilities accorded to land-locked States and generalized systems of preferences which, despite the word "generalized", were limited to particular spheres.

30. In addition, proposals had been submitted by EEC (A/CN.4/308 and Add.1 and Add.1/Corr.1, sect. C, 6, para. 6) and ECWA (*ibid.*, sect. B). In its comment, ECWA had suggested that it might be advisable either to make the draft article more general, with no specific reference to the GSP, or to expand it to include other forms of preferential treatment for developing countries. It had also pointed out that the article neglected to mention preferences granted among developing countries.

31. Article 21 of the Charter of Economic Rights and Duties of States made it quite clear that an exception should be made for trade preferences granted by developing countries to other developing countries, and also provided that, in those cases, developing countries should not be obliged to extend such preferences to developed countries.

32. In the light of those considerations, he hoped the Commission would consider enlarging the scope of the article, even though the underlying idea was sound. It was also necessary to take account of the views expressed in the Sixth Committee of the General Assembly regarding the need to include further exceptions in favour of developing countries. Mr. Njenga had already made a proposal in that sense, and the Special Rapporteur had himself said that new articles relating to developing countries could be introduced, in addition to articles 21 and 27.

33. Mr. TABIBI said it would be very helpful if the Secretary-General of UNCTAD or, failing him, the UNCTAD official responsible for preferences, were invited to attend the Commission's meeting on that question and make a statement, with special reference to the important events that had occurred since 1975. He suggested that the secretariat of the Commission should get in touch with UNCTAD to see whether that was possible.

34. Mr. FRANCIS trusted that Mr. Tabibi's suggestion would be without prejudice to his own earlier suggestion[16] that UNCTAD should be invited to submit written comments on the draft articles on the most-favoured-nation clause. It was a delicate matter, on which the General Assembly, as well as the Commission, would like to have UNCTAD's reaction.

35. The CHAIRMAN said that the Secretary to the Commission would approach the Secretary-General of UNCTAD on the matter.

The meeting rose at 1 p.m.

[16] See 1484th meeting, para. 30.

1495th MEETING

Wednesday, 7 June 1978, at 10.05 a.m.

Chairman: Mr. José SETTE CÂMARA

Members present: Mr. Ago, Mr. Calle y Calle, Mr. Dadzie, Mr. Díaz González, Mr. El-Erian, Mr. Francis, Mr. Jagota, Mr. Njenga, Mr. Quentin-Baxter, Mr. Reuter, Mr. Riphagen, Mr. Šahović, Mr. Schwebel, Mr. Sucharitkul, Mr. Tabibi, Mr. Tsuruoka, Mr. Ushakov, Sir Francis Vallat, Mr. Verosta.

The most-favoured-nation clause (*continued*) (A/CN.4/308 and Add.1 and Add.1/Corr.1, A/CN.4/309 and Add.1 and 2)

[Item 1 of the agenda]

DRAFT ARTICLES ADOPTED BY THE COMMISSION: SECOND READING (*continued*)

ARTICLE 21 (The most-favoured-nation clause in relation to treatment under a generalized system of preferences)[1] (*continued*)

1. Mr. SCHWEBEL said that, while there was obvious merit in the objectives of the GSP, it was not certain whether those objectives would be attained in practice, especially as the effect of such preferences was diluted by other derogations from the most-favoured-nation clause.

2. There were a number of questions to be answered. For example, of what significance were generalized preferences for the State trading economies, where all imports were brought in by a State agency? And, in other economics, whom did they benefit? Were the commodities covered by preferences available to consumers in developed countries at lower prices, or were the profits siphoned off by middlemen? Did the system not tend to favour the most developed of the developing countries? And, in the developed countries, did it not place an unfair

[1] For text, see 1494th meeting, para. 1.