Chapter III

The Establishment of the Customs Union

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I. INTRODUCTION

The European Economic Community is, above all else, a customs union. The provisions of the Treaty establishing it which directly relate to the customs union make up, it is true, only forty-odd of its two hundred and forty eight articles. Nevertheless, the point of departure of the Treaty doubtless was and remains the establishment of a customs union.

A customs union groups countries each having a national geographic and economic area generally protected at the outset by customs barriers and, with regard to certain products, by import quotas vis-à-vis the rest of the world. These countries agree to eliminate among themselves customs duties and quotas, and thereby to form a single territory within which goods may circulate wholly without obstacles, regulation or limitation. Commercial unification of such a group of countries also involves agreement to enforce, within the newly-unified territory, a single tariff schedule which, vis-à-vis the rest of the world, replaces national tariffs. This common external tariff must at the same time be combined with a common commercial policy vis-à-vis non-member countries.

The elimination of the obstacles to trade among the countries which thus form a customs union, and the establishment of an external tariff common to its members necessitate a series of progressive steps. The importance of a step-by-step progression is increased whenever differences among the points of departure of member countries are pronounced.

In the case of the European Economic Community, the problem is to establish a customs union among the following:

1) The three Benelux countries (Belgium, the Netherlands, and Luxembourg), who have already established a customs union among themselves, which has been in existence since 1950. In that year these three countries abolished customs duties among themselves at a single stroke and adopted a common external tariff. On the other hand, the elimination of quotas on their mutual trade (even today there still exist a few) and the creation of a single list of liberated goods in regard to imports from member countries of the Organization for European Cooperation (O.E.E.C.) and from the rest of the world required several years. A list of liberated goods was established in 1956 valid for imports from O.E.E.C. countries, but no similar list is yet in force in regard to imports from certain non-O.E.E.C. countries. The general level of tariff protection in the Benelux countries is quite low, although their duties on certain manufactured products are relatively high. These countries are poor in raw materials and to a large extent have traditionally depended for economic survival upon foreign commerce. Their imports per capita average $450.00 annually and their exports $400.00.

2) Germany, a country whose tariffs in the past have been fairly high. In keeping, however, with Professor Erhard’s policy of freeing its economy from controls, Germany has, since 1955, reduced its tariffs of its own accord, and is therefore considered today as having relatively low tariffs. Germany is characterized by its highly dynamic policy of commercial expansion. Per capita imports attain a yearly average of $200.00, and exports of $250.00. Germany’s quota policy is also a very liberal one. Because her balance of payments is flourishing and her exchange reserves are considerable, she has progressively eliminated almost all quotas on imports from countries of the non-communist world.

3) Italy, whose foreign commerce represents a smaller share of national income—per capita imports averaging $80.00 yearly and exports $80. Italy has, however, systematically developed her foreign trade, especially since the war, to a point where she is emerging as a great commercial country. She very early adopted a remarkably liberal policy in regard to quotas on imports from European countries. In fact, she has since 1950 removed almost all quotas on imports of goods produced in the member states of the O.E.E.C. Her restrictions on goods from other countries are stricter, but these
are now being progressively removed. Italy is considered to be a high-tariff country, even though she has unilaterally suspended duties in a very substantial degree.

4) France, which, because of traditionally protectionist attitudes and balance-of-payments difficulties, maintains both a very rigid system of import quotas and high tariffs. Foreign commerce generates a relatively small portion of France's national income, imports averaging $180.00 per capita annually and exports $170.00. Since the end of 1958, however, France has pursued a policy of progressive elimination of quotas on imports from O.E.E.C. countries, a policy which will in the future be applied to imports from other countries.

Among countries whose situations are so disparate at the outset, unusual efforts are required to achieve the elimination of obstacles to the exchange of goods and the establishment of a common external tariff as well as of a common commercial policy vis-à-vis third countries. The economies of these countries can be subjected only progressively to foreign competition. More abrupt changes in competitive conditions would create the risk that economic activity (which in one of the Six had always been protected either by high tariffs or quotas or both against foreign competition, including the competition of its new partners within the Community) would be endangered by the competition of similar activity of the other members of the Six. The goals of the Common Market, it is true, are to stimulate a better division of labor among the Six, to increase productivity and the like, but the sudden disappearance of any significant economic activity within a Member Country would create economic, financial, and social problems which the Community would not survive.

This emphasizes the necessity of proceeding slowly in order to extend the impact of the consequences of coordination of the industries of the Six over a period of time. Clearly this necessity is more imperative for those countries of the Six which at the beginning enjoyed the protection of the highest tariffs and quotas. To the Benelux countries, which enforced few quotas and low tariffs and were therefore accustomed to world competition (with the exception of a few Benelux industries which enjoy greater than average protection), the deliberation with which the Community will be created is less important than to France.

A "transitional period" of twelve to fifteen years beginning on
January 1, 1958, was therefore agreed to in the course of which the customs union is to be progressively created. During this transitional period, the Six are to undertake to:

1) abolish altogether tariffs among themselves,
2) abolish all import and export quotas on trade among themselves,
3) establish a common external tariff,
4) establish a single list of quota-free imports from non-member countries and, as to products which are not free from quotas, adopt a common quota policy.

In addition and concurrently, other more technical measures must be taken. For instance, methods of applying customs duties are to be unified: a common tariff is not adequate if methods of evaluation in Hamburg, Rotterdam, Marseilles, and Genoa differ. It is therefore appropriate not only to fix common tariffs but also to establish common rules for the application of such tariffs. In short, customs rules and regulations in their entirety must be unified.

But the solution of tariff and quota problems requires contemporaneous settlement of a great number of other questions as well. The problem of coordinating basic economic policies aside, steps closely connected with the elimination of tariffs among members of the Six include the establishment and enforcement of equitable rules of competition, and the harmonization of fiscal legislation affecting imported products. These problems, all of foremost importance, are in part treated elsewhere in this book. These remarks are merely intended to emphasize the fact that, even though the rules directly relating to the customs union constitute only forty or so of the two hundred and forty-eight articles of the Treaty, the majority of the other provisions contribute to its creation.

A direct connection has, moreover, been established between the progressive formation of the customs union and the other steps which are related to it. This connection is a characteristic of each of the stages of the transitional period.

The Treaty provides that the Common Market shall be established in the course of a transitional period of twelve years divided into three stages of four years each. It further provides that, "to each stage there shall be allotted a group of actions which shall be undertaken and pursued concurrently." This provision ensures the necessary contemporaneity between the creation of the customs

1 European Economic Community Treaty art. 8. The E.E.C. Treaty is generally referred to herein as "the Treaty."
union in the strict sense of that term and other measures, like harmonization of fiscal legislation, to which reference has already been made. In addition the Treaty provides that a condition of the progression from the first to the second stage of four years shall be confirmation that the purposes envisaged for the first stage have in their essentials been achieved and that the obligations incurred by the Member States in accordance with the terms of the Treaty have been fulfilled. These objectives and obligations are, of course, those related to the initial creation of the customs union, but they also include those not specifically related to tariffs and quotas.

At the end of the first stage a statement shall, subject to the unanimous agreement of the six Member States, be issued that the objectives have been reached and the obligations fulfilled. If unanimity cannot be achieved, the first stage shall automatically be extended for a period of one year. At the end of this year (the fifth after the coming into force of the Treaty) the Six shall again seek a unanimous vote that the obligations fixed by the Treaty have been effectively fulfilled. If unanimity still cannot be achieved, the first stage shall be extended for a further period of one year (the sixth). At the end of this further year the vote of a majority of the Member States shall decide. If no majority can be obtained, the Member States shall designate an arbitration board to determine whether the required statement should issue. Its decision shall bind the Member States.

What would result if the arbitration board decided that the obligations had not been fulfilled? The Treaty is silent on this question. Clearly, however, in such a case the extremely serious political situation resulting would bring about either a complete failure of the Treaty, or the Member States, on the highest governmental level, would be forced to take political measures to save the situation.

If, as a result of a unanimous vote at the end of the fourth or the fifth year, or of a majority vote at the beginning of the sixth year, or of a decision by the arbitration board, the statement is issued that the objectives of the first stage have been attained, the Member States must proceed with the execution of the second stage. The Treaty is silent on the transition from the second to the third stage; therefore it is to be assumed that this transition is automatic. The Treaty also provides that the second or the third stages may not be extended or curtailed, except pursuant to a unanimous decision of the Council.

The Treaty further declares that the provisions which may permit the extension of the first stage in the manner described, or those which permit modification of the duration of the second and third stages, shall not have the effect of extending the transitional period beyond fifteen years. Consequently, the customs union among the Six should become a reality in all particulars in the period between December 31, 1969, and December 31, 1972.

Obligations arising from the Treaty do not excuse the Six from meeting outstanding national obligations which individual Member States may owe to other countries. The substance of these obligations is contained in the General Agreement on Tariffs and Trade (G.A.T.T.) of which each of the Six is a signatory. This Agreement, to which about forty countries on six continents are parties, establishes a number of rules which bind the signatories in fixing commercial policy. The basic philosophy of the Agreement is that reflected by most-favored-nation clauses. If certain countries decide to abolish tariffs among themselves, without extending such benefits to the other signatory countries, the most-favored-nation principle is obviously not respected with regard to those countries. The G.A.T.T., however, authorizes the formation of customs unions, but it stipulates specific conditions with a view to giving certain guarantees to those contracting parties of the General Agreement who are not to be union participants. The Six must respect those conditions in establishing the Common Market, and these same conditions will govern, to a large extent, the commercial policy of the new Community towards the rest of the world.

The two categories of actions to be taken by the Six—those designed to abolish the obstacles to trade among themselves, and those designed to establish a common external tariff and a common commercial policy—conveniently define an outline of a study of their customs union. Part II of this chapter will therefore be devoted to relations of the Six with one another and Part III to the relations of the Six with third countries. Agricultural and food products will not be considered. Although it is true that basic principles are the same whether these or industrial products are at issue, the means of giving effect to such principles where agricultural and food products are concerned differ somewhat. The measures envisaged are, moreover, not so clearly defined as those in the area of industrial products since the Treaty generally leaves them to be spelled out and implemented by decisions of the Community institutions.

*Treaty art. 234.*
II. RELATIONS AMONG THE SIX

A. ABOLITION OF TARIFFS

The Treaty provides that tariffs shall be frozen as of the date of the entry into force of the Treaty. Consequently, since January, 1958, the Six have no longer had the right to raise their tariffs vis-à-vis each other.

1. THE BASIC CUSTOMS DUTIES TO WHICH THE TREATY RULES APPLY

The tariffs to which the rules governing the abolition of tariffs are to be applied are precisely defined. The Treaty calls these tariffs "basic duties," and provides that the basic duties which are subject to successive reductions are those applied on January 1, 1957. This means that the "freeze" applies to duties actually in force on January 1, 1957. More precisely, if a country had increased its customs duties between January 1, 1957, and the date of the first tariff reduction (January 1, 1959), it was obliged at that date to revert to the level in force on January 1, 1957, and to use this level as the basis for the reductions provided for by the Treaty.

This rule is all the more strict since the basic duty is the one that was in fact applied on January 1, 1957. If, at that date, a country had temporarily suspended, either in whole or in part, a customs duty previously obtaining, the basic duty would be the tariff actually collected on merchandise on January 1, 1957, taking into account the suspension, and not the tariff which would have been applicable had there been no suspension. This interpretation of the provisions of the Treaty has been confirmed in particular by the ruling of the Commission directed at France, which in 1958 had re-established a customs duty on paper pulp which she had suspended in 1957. The Commission ruled that France must abolish the re-established duty.

2. THE TIMING OF THE PROGRESSIVE ABOLITION OF CUSTOMS DUTIES

The timing of the progressive abolition of customs duties among the countries of the Community is determined as follows:

1) In the course of the first stage of four years, the first reduction

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4 Treaty art. 12.
5 Treaty art. 14.
6 Ibid.
was to be made one year after the date of the entry into force of the Treaty (that is, on January 1, 1959); the second reduction is to be made eighteen months later (on July 1, 1960); the third reduction is to be made at the end of the fourth year (on January 1, 1962).

2) In the course of the second stage (which may begin either immediately after the first stage, or one or two years later, or even a little later) a reduction is to be made eighteen months after the beginning of the second stage, a second reduction eighteen months later, and a third reduction one year later. If it is assumed that the second stage will begin immediately after the end of the first stage, the reductions of the second stage will occur on July 1, 1963, January 1, 1965, and January 1, 1966, respectively.

3) The reductions which still remain to be made at the end of the second stage are to be carried out in the course of the third stage, according to a time-table to be determined by a majority of the Council of Ministers of the Community.

The amount of the tariff reductions is determined in the following manner:

1) At the time of the first reduction (which was effected on January 1, 1959) all tariffs (i.e., the basic duties) between Member States of the Community were to be reduced by 10%.

2) At the time of each subsequent reduction, each Member State is to reduce the total of its customs duties towards its partners in the Community in such a way that its “total customs receipts” will be reduced 10%, it being understood that the reduction of duty on each item shall be equal to at least 5% of the basic duty.

The “total customs receipts” are to be calculated by multiplying the value of the imports of each Member State from other Member States during the year 1956 by the basic duties. The “total customs receipts” provide a basic point of reference which remains unchanged throughout the period during which the Treaty is in effect. Each country within the Community has therefore established this figure by applying to a table of its imports for the year 1956 the relevant customs duty in effect on January 1, 1957 (basic duty). The sum of the products of the multiplication of these two elements is the “total customs receipts.” With each reduction pursuant to the Treaty, each country must reduce customs duties in this table to the extent necessary to ensure that the application of the new duties will result in a 10% reduction of the “total customs receipts.”
ceipts." The new duties thus arrived at are to be applied to imports of 1960, 1961, and so forth.

3. FLEXIBILITY OF THE RULES ABOLISHING INTERNAL TARIFFS

The first reduction—that which took place on January 1, 1959—is therefore the only one which involves a diminution of 10% of each customs duty. A reduction of 5% of each customs duty is thereafter obligatory each time reductions are to be made, but each country remains free to choose those duties which will be reduced more drastically in order to achieve a reduction of total customs receipts of 10%. It would seem, however, that the Six plan an equal all-round reduction on July 1, 1960. The freedom thus given to Member States exemplifies the flexibility of the Treaty system of tariff reductions. In effect it permits each country to maintain for as long a period as possible customs protection of products with regard to which it most fears the competition of other Member States. In the course of the first two stages six reductions are thus contemplated which are to reduce the total customs receipts by 60% as compared with the duties in force on January 1, 1957. A country can, by applying the minimum reductions to a given product, that is 10% at the first reduction, and 5% at each of the five subsequent reductions, keep reduction of tariff protection of that product to a minimum 35% as of the end of the second stage. This means of course, on the one hand, that it shall have applied a reduction as to other products which exceeds 60% in order that the over-all reduction of total customs receipts shall equal 60%, and on the other hand, that the efforts to be made in the course of the third stage with regard to products enjoying the greatest amount of protection during the first two stages will be greater.

Consequently, at the end of the second stage, and solely on the basis of the rules described above, the level of over-all tariff protection of each Member State will have been reduced to one which is 40% of the initial level. With regard to certain products, however, the level may still be as high as 65% of the initial level, the level with regard to other products being, correspondingly, less than 40% of the initial level.

4. SAFEGUARDS AGAINST EXCESSIVE FLEXIBILITY

To avoid, however, the situation which might result at the end of the second stage—namely, that the Member States will have maintained a degree of tariff protection which cannot be abolished
in the third stage without creating serious difficulties—the rules elaborated above are supplemented by three provisions:

1) On the one hand, it is provided that duties exceeding 30% at the time of any reduction must be reduced at least 10%. Therefore any duty remaining above 30% is deprived of the benefits of the rules creating flexibility. If, as a result of any reduction, the duty falls below 30%, the rules creating flexibility are then applicable to it and the minimum reduction is thereafter 5%.10

2) On the other hand, goals are established for Community countries. They must endeavor to arrive at a reduction of the duties on each product amounting to at least 25% of the basic duty at the end of the first stage, and at least 50% at the end of the second stage. The Commission may make recommendations to Member States to encourage them to achieve these goals.11

3) Finally, the Member States, having declared their willingness to reduce tariffs among themselves more rapidly than provided for in the rules—if general economic conditions and the situation of the industrial sector concerned so permit—the Commission may, with this end in view, make recommendations to the Member States.12

As suggested,13 the timing of reductions remaining to be achieved at the end of the second stage is not fixed by the Treaty. The Council must determine such timing at the appropriate moment. In principle, only the timing itself should thus be defined, the system of reduction continuing to be as flexible as it is in the first two stages (the first reduction of the first stage apart). But it must be emphasized that the Member States have incurred an unconditional obligation to abolish completely customs duties among themselves by the end of the third stage.14 Even though there is a right, therefore, to invoke the rules creating flexibility as a matter of law, this right will become more and more illusory in fact. For instance, if a country has, with regard to a given product, made full use of the flexibility of the system in the course of the first two stages, and maintains on that product at the beginning of the third stage a duty which is 65% of the basic duty which obtained on January 1, 1957, it will necessarily be obligated to eliminate this 65% within the four years of the third stage.

10 Ibid.
11 Ibid.
12 Treaty art. 15.
13 See note 7 supra.
14 Treaty art. 13.
5. METHODS OF IMPLEMENTATION ON JANUARY 1, 1959, OF THE RULES ABOLISHING INTERNAL TARIFFS

The uniform 10% reduction on January 1, 1959, of customs duties among Member States pursuant to the Treaty caused no difficulties. In fact, implementation proved to be remarkably simple. Implementation of the Treaty rules in subsequent stages will be complicated to the extent that Member Countries, seeking to postpone the day when certain sectors of their economies must forego tariff protection, invoke the rules creating flexibility. Obviously special interest groups in each country may try to convince their governments that their economic activities, more than any others, need the maximum protection permissible and for as long a period as possible. On the other hand, many industries—having strenuously prepared to meet new competition in the Common Market, and having invested heavily to this end—are now interested in speeding up the removal of economic frontiers so that they may more rapidly obtain access to a larger market and a return on their investments.

On January 1, 1959, each Member State effected, then, a 10% reduction of its tariffs vis-à-vis other Community countries. Because of Germany's unusually favorable balance of payments and in keeping with the liberal policies pursued by Dr. Erhard, during 1957 she unilaterally reduced tariffs on a substantial number of imports from the rest of the world. Given the fact that the basic duty of the Treaty is the duty in force on January 1, 1957, Germany was under no obligation to reduce tariffs on imports from other Member Countries on January 1, 1959, where it had already reduced them more than 10% of the basic duty during 1957. As a result, Germany was obliged to reduce customs duties on January 1, 1959, only on a few products, notably those on textiles and leather.15

6. TECHNICAL PROBLEMS OF THE IMPLEMENTATION OF THE RULES ABOLISHING INTERNAL TARIFFS

The Treaty also provides 16 that taxes having an effect equivalent to that of customs duties shall be progressively abolished during the transitional period. No definition of such taxes is given, however. The Commission is to define them, and to determine the means and

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15 The difficulties encountered by France arising from the fact that it had not correctly determined its basic duty on paper pulp have already been mentioned.
16 Treaty art. 13.
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timing of their abolition; in doing so it is to be guided by the Treaty
rules governing the abolition of customs duties. The Commission
has not yet collected the necessary information from industry with
regard to taxes which have an effect equivalent to that of customs
duties and which may be in effect in Community countries. No spe-
cific measures have been taken, therefore, with respect to taxes.

In connection with the relations of the Six to one another, one
problem arises which has so far been only rarely discussed: that of
customs evaluation. When products are to be imported, the customs
authorities examine the documents which the importer (or his
agent) produces to establish the price of the products. When the
authorities decide, on the basis of these documents, that the de-
clared price is reasonable, was freely negotiated by the buyer and
the seller, and has been correctly declared, they accept it and cal-
culate the duty with that price as a base. In all Community coun-
tries customs authorities enjoy, however, a very large measure of
discretionary power. They may decide—virtually without being
required to give any justification therefor—that the declared price
is too low, and they may themselves fix another price as the basis
upon which the duty to be paid is determined. By systematically in-
creasing prices declared by importers, customs authorities could,
therefore, partially annul the effects of customs reductions to be
achieved in keeping with the Treaty. Given the customs laws pres-
ently in force in the Six, importers would have few ways of combat-
ting such arbitrary action, even though international conventions,
and in particular those elaborated by the Council of Customs Co-
operation, have established certain rules concerning the calculation
of values for customs purposes. Customs authorities do not, how-
ever, appear to have misused their powers up until now, and no com-
plaint seems to have been voiced by any of the Community countries.
It should also be noted that as the customs reductions increase with
the passing of the years, increases in customs evaluation would be
less and less effective as a means of defeating the intended effects of
the Treaty.

Such is the rather complex system created by the Treaty for the
abolition of tariffs among the Six. It has the advantage of being
flexible enough to permit each country to maintain protection of its
most vulnerable industries for longer periods of time. The obvious
disadvantage of this flexibility is that, if the Member States take
full advantage of it, final tariff reductions will be particularly diffi-
cult for industries which continue to enjoy protection unless the
respective countries also take advantage of the first years of the transition period to reorganize or convert them effectively.

B. THE ABOLITION OF QUOTAS

1. THE RULES OF THE ORGANIZATION FOR EUROPEAN ECONOMIC COOPERATION

Since its creation in 1948 the Organization for European Economic Cooperation (O.E.E.C.) has endeavored to abolish import quotas among the seventeen member countries of Western Europe. The obligations of these countries, which O.E.E.C. imposed with a view to abolishing quotas, have taken the form of “percentages of liberalization.” A “year of reference,” the year 1948, was chosen, and each country agreed to abolish, on specified dates, quotas on a given list of products. This list was to be determined according to the following formula: the volume of 1948 imports of the products included in the list from other Member States (and their territories) must at least have equalled a determined percentage of the total volume of all products imported by the country in question in 1948 from the other Member States (and their overseas territories). Having fixed this minimum percentage at 50% in 1949, 60% in 1950, 75% in 1951, the O.E.E.C. raised it to 90% in 1955.

The Six are all members of the O.E.E.C. and as such they have been—and remain—subject to these rules. With the exception of France, each of the Six has of its own accord adopted, and even gone far beyond, the minimum percentages of liberalization established by the O.E.E.C. Germany had thereby achieved liberation of 91.8% of her intra-European trade, the Benelux countries 95.6%, and Italy 98.4%. France, on the other hand, was forced to invoke, in June, 1957, the safeguard clauses to which O.E.E.C. obligations are subject; until December 1958, she therefore applied a global quota on imports from O.E.E.C. countries, including those from Community countries. In December 1958, in conjunction with the return to partial convertibility of European currencies, and as a result of the program to achieve sound economy and finance initiated by the government of General de Gaulle, France also liberalized 90% (based on 1948) of its imports originating from other O.E.E.C. countries.

On January 1, 1959, therefore, only a relatively small percentage of imports from one of the Six were subject to quotas in another of the Six. This percentage varied, however, from country to country,
and the kinds of goods involved varied greatly. Generally the imports still subject to quotas were those which, in the view of the governments concerned, would have endangered domestic production of similar products if no quotas had existed.

Germany, the Benelux countries, and Italy maintained quotas only on a limited number of imports of industrial products. On the other hand, France, even though she had liberalized more than 90% of her imports compared with 1948, applied quotas to a large list of products. If quotas on these goods had been removed, imports would doubtless have increased greatly and would have represented much more than 10% of French imports. These facts explain the rules of the Treaty concerning the abolition of import quotas. As will become clear in the following discussion, developments have proved that the authors of the Treaty were, in this regard, overly pessimistic.

2. THE RULES OF THE TREATY

As is true in the case of tariffs, the Treaty provides, first of all, that quotas be frozen as of the effective date of the Treaty.17 This measure takes two forms:

1) on the one hand, the reinstatement of quotas which had been abolished as of January 1, 1958, is prohibited, and

2) on the other hand, a quota may not be made more restrictive—in other words, the level of imports envisaged by the quota may at no time be reduced.18

These rules apply, of course, only among Member States. Each country is perfectly free to reinstate quotas vis-à-vis third countries, or to make them more restrictive.

The Treaty provides, moreover, that quotas are to be totally abolished by the end of the transitional period.19 To this end, the Treaty provides that:

1) each Member State shall, one year after the Treaty takes effect, convert bilateral quotas into global quotas open, without discrimination, to all other Member States.20 European countries which maintain quotas on given products generally do not, in fact, fix them unilaterally. Quotas are negotiated with each European supplier country, and each negotiating party attempts to gain as great an advantage as possible for its exports to the markets of the other

18 Treaty art. 32.
19 Ibid.
20 Ibid.
while increasing as little as possible quotas on the sales of the other's goods in its own markets. Accordingly, if the quid pro quo which country A receives from country B is larger than that from country C, country A will open a larger quota to country B's goods than to those of country C. Discrimination exists as between countries B and C in the market of country A, therefore. The globalization of quotas or, in other words, the transformation of bilateral quotas on the same product, each of which is open to one country, into a single quota open to all will put an end to such bargaining, abolish bilateral negotiations, and assure, in principle, non-discrimination.

2) The global quota must at least equal the sum of the bilateral quotas previously applicable to that product. Moreover, when each state has globalized its bilateral quotas, it must increase the total of its global quotas to such an extent that their total value as compared with the preceding year is increased not less than 20%, it being further understood that the global quota for each product must be increased by not less than 10%.

3) The global quotas must be increased each year in accordance with the same rules and in the same proportions (20% of the total value of the preceding year's global quotas and a minimum of 10% per quota).

4) The fourth increase of the quotas shall take place at the end of the fourth year after the Treaty becomes effective, and, taking account of the problem of the transition from the first to the second stage of the transitional period, the Treaty further provides that the fifth increase shall take place one year after the beginning of the second stage. Therefore, if the first stage is extended, as is permitted, there will be no increase of quotas during the period of the extension.

3. FLEXIBILITY OF THE TREATY RULES AND THE SAFEGUARDS AGAINST EXCESSIVE FLEXIBILITY

As is true of the rules concerning tariffs, the rules in regard to the elimination of quotas are flexible. This results from the fact that each country, although obligated to increase by 20% each year the total volume of its quotas, may limit the increase to 10% in connection with goods of its own industries which have reason to fear a too-rapid growth of foreign competition. If a Member State does so, however, it must increase to a greater extent its remaining quotas

21 See note 7 supra.
in order to attain the required over-all increase of 20% of its quotas.

It became evident, however, that these rules might not prove adequate to bring about a total liberalization by the end of the transitional period. It was, in fact, difficult to measure the degree of restrictiveness of any particular quota and to say whether its annual increase by 20% over the preceding year for a period of twelve years would certainly result in the total liberation of the product from quotas by the end of the transition period. For this reason these rules have been supplemented by a number of other provisions.

In the first place, special rules have been established for low or nonexistent quotas. The Treaty provides that if, for a product which cannot be freely imported, the global quota does not amount to 3% of the national production of the nation concerned, a quota equal to not less than 3% of such production shall be established one year after the date of the entry into force of the Treaty (that is, on January 1, 1959). This quota is to be raised to 4% at the end of the second year (i.e., on January 1, 1960), and to 5% at the end of the third year (i.e., on January 1, 1961). Thereafter, the State concerned must increase the quota by not less than 15% annually. The Treaty also indicates that in the case where there is no national production, the Commission must fix an appropriate quota.

By these special procedures, the drafters of the Treaty intended to establish quotas at relatively high levels at the outset in the hope that at the end of the transitional period there would be every chance that the affected products could be freed of quotas or that such liberation would create no problems. The establishment of such points of departure was obviously necessary in the case of certain countries which today, in effect, prohibit the importation of certain products. For such products the annual global increase of 20% and the 10% increase per quota would not have sufficed to assure liberalization after the twelve quota increases.

In the second place, the Treaty provides that, at the end of the tenth year of the transitional period, each quota shall be equal to not less than 20% of the national output of the product in question. This rule strengthens even further the rules concerning low or nonexistent quotas, since, the application of the other rules relating to them would not normally raise quotas higher than 13.3% of the national production at the end of the tenth year of the transitional period.

22 Treaty art. 33.
23 Ibid.
24 See note 22 supra.
In the third place, the Treaty contemplates that, if in the light of experience, the Commission finds that the rules concerning the progressive abolition of quotas, and in particular the rules relating to percentages, do not assure the complete abolition of import quotas at the end of the transitional period, the Council may, pursuant to a proposal of the Commission, modify these rules and, specifically, may raise the percentages. Decisions of the Council must be made by a unanimous vote during the first stage, and thereafter by a majority vote.

Finally, as is true of the abolition of tariffs, the Member States have declared their willingness to abolish import quotas, in relation to other Member States, more rapidly than is provided for by Treaty rules if general economic conditions and those relevant to the economic sector concerned so permit.  

Another quite interesting rule concerning the abolition of quotas should be mentioned. It provides that, in case the Commission finds that in the course of two successive years the imports of any product have been below the level of the quota fixed for it, this quota may not be taken into consideration for the purpose of calculating the total value of global quotas. In such a case, the interested country must liberate the product in question. If no such rule existed, a country could, in order to achieve the 20% over-all annual increase of quotas for which the Treaty provides, effect a considerable increase in the quota on a product for which it knows that the domestic demand is small with the certainty that no imports of consequence would result. This would avoid the necessity of increasing quotas on products for which a strong domestic demand exists—increases which would result in a larger volume of imports. It is a rule which, in a sense, is designed to prevent fraudulent calculations of quota increases.

4. IMPLEMENTATION OF THE RULES ELIMINATING QUOTAS ON JANUARY 1, 1959

The application of these rules on January 1, 1959, created a great number of difficulties and a great number of problems had to be resolved in order to give them effect. At first they did not seem to have been observed in all countries to everyone’s satisfaction, and complaints were fairly frequent. The net result, however, of the initial application of these rules has been definite progress. More-
over, the return of European currencies to convertibility, as will become clear, set off a much faster movement towards the elimination of quotas, which has made the problem far less acute, not only among the Six, but also between them and the rest of the world.

Each country had, at the outset, to establish a "quota framework"—a list of products still subject to quotas in the country concerned. Opposite each of the products on this list the country indicated the bilateral quotas it had granted to other Community countries in the course of 1958, as well as, for each product, the global quota that was to be established in the course of 1959, pursuant to the provisions of the Treaty.

For the purpose of calculating the quota for 1959, the rules of the Treaty were applied in the following manner:

1) In the first place each country increased by 10% on each product the total of the quotas granted to other Community countries in the course of 1958.

2) With regard to those products on which no quota had been opened in the course of 1958, or on which the quotas opened in 1958 were, in sum, inferior to 3% of the national production of the product in question, the country fixed a quota equal to 3% of its national output. Generally, this resulted in quotas far higher than 10% of the total of comparable quotas opened in 1958.

3) The country in question then compared, with reference to the total volume of products under quota, the total of the quotas opened in 1958 with the total of the quotas opened in 1959, taking into consideration the rules cited in paragraphs 1) and 2) above. If the sum total of the quotas of 1959 was higher by at least 20% than the sum total of the quotas of 1958, the country was considered as having accomplished its obligations within the terms of the Treaty. If the sum total of the quotas of 1959 was not higher by 20% than the sum total of the quotas for 1958, the country, in order to fulfil its Treaty obligation to effect a 20% over-all increase, had to increase some quotas. Each country was free to choose those products whose quotas were to be increased.

The application of these rules, and especially of the 3% rule, has, in fact, led two countries of the Community to increase by much more than 20% its aggregate quotas of 1958. France, whose 1958 quotas reached the sum total of one hundred billion francs, increased its quotas in 1959 to two hundred-fifteen billion francs, or by 115%. Italy increased them to twenty-eight billion lire in 1959, compared with the eight billion lire in 1958, an increase of 250%.
The application of the 3% rule had noteworthy results with regard to certain products, for instance, passenger cars. The national production of cars in Italy and France is substantial, and until 1958 both pursued a very restrictive import policy. As a consequence of the 3% rule, France increased the quotas open to other Community countries from four-and-a-half billion francs in 1958 to seven billion in 1959, and Italy her quotas from three-and-a-half billion lire in 1958 to five billion in 1959. In the Benelux countries and Germany which, in general, followed liberal policies in regard to industrial imports even before the Treaty came into force, the rule of 3% has been only rarely applied, and the increases of 1959 quotas over those of 1958 were not much higher than the 20% fixed by the Treaty, at least they were not in connection with industrial products. No decisions have been reached in regard to products of which there is no national production and in connection with which the Commission therefore must fix quotas.

5. TECHNICAL PROBLEMS OF THE IMPLEMENTATION OF THE RULES ELIMINATING QUOTAS

The application of the quota rules caused great difficulties, and protests of producers, importers, and exporters of the Community against the manner in which given countries implemented the rules, either in whole or in part, were frequent early in 1959. Criticisms were directed particularly at the conditions under which the 3% rule was applied and against the way in which global quotas were handled.

With respect to the rule of 3%, the difficulty obviously lies in determining national production. Certain countries demonstrated a strong tendency to make use of every available means of reducing the valuation of their national production with a view to reducing the amount of the 3% quotas. Long discussions have been conducted within the Community in an effort to determine the following:

1) Should the production be calculated by quantity or by value, calculation by value generally permitting more arbitrary figures than calculation by quantity?

2) Is that part of the production of a given product not utilized as such, but incorporated as a component part of another product, deductible? For instance, should the quota to be opened be 3% of the entire national output of car tires or should it be 3% of car tire production marketed as such, deducting that part of tire production which is mounted on new cars, since the latter have obviously been
figured in the calculation of car production and its corresponding quota?

3) May a country deduct from the value of its national production the amount of customs duties which would have been paid with respect to such products had they been imported instead of being produced within the country? The reason for this question is the fact that the comparison between national production and imports should take into account the disparity in costs of goods produced domestically and of those produced abroad which results from the duties payable by the latter. The Commission decided to authorize a fixed reduction of a maximum of 20% of the value of national production in order to take this factor into account.

4) In calculating the value of production, should deductions be made for all indirect taxes?

The result of the various methods used in certain countries to achieve a systematic reduction of national production values was that the quotas opened in 1959 on certain products were less than half what they would have been had the calculation been based on quantities.

A particular problem resulting from the devaluation of the French franc in December 1958 must be noted. France calculated her quotas in French francs, and this, in view of the devaluation, had the result of reducing by 15% the value of authorized imports calculated in foreign currencies.

The administration of global quotas also created difficulties—for example the issuance of licenses was delayed or limitations were placed on the periods of time within which they may be used. Some importers feared that licenses which had not been used as of December 31, 1959, would be annulled, even though their issuance was so delayed that it would have been materially impossible to effect the relevant imports within the period of time for which the licenses were valid. Moreover, even though distribution of licenses should be non-discriminatory, complaints have occasionally been heard that, within given quota categories, a large proportion of the total value of the licenses issued was for products having only a few potential buyers (for example, luxury passenger cars), while the total value of licenses in the same quota categories for products which are much in demand (for example, popularly-priced passenger cars) was very low.

These difficulties are fairly serious. Nevertheless, in general the application of the Treaty clearly has initiated an irreversible move-
ment towards the abolition of quotas among the countries of the Community. Community authorities have made every effort to carry out the provisions of the Treaty as faithfully as possible, but at the same time they have been relatively tolerant in those instances where certain provisions of the Treaty, especially the 3% rule, in fact imposed an extremely heavy burden on the importing country because of the risk of serious difficulties for its industries. The country concerned could in such cases invoke the safeguard clauses, but, for fairly evident psychological and political reasons, partisans of the Treaty wished from the outset to avoid crises which might justify resort to these clauses. The initial implementation of the Treaty was greeted with some enthusiasm in Europe, and it would be extremely regrettable if this enthusiasm were dampened by social or other crises. Prudence is therefore advisable during the early stages.

Moreover, it should be noted that, as mentioned above, the provisions of the Treaty concerning the abolition of quotas will gradually lose their raison d'être as trade is progressively liberalized on a world-wide scale, notably under the stimulus of the International Monetary Fund and the G.A.T.T. This aspect of the problem will be dealt with in the second part of this chapter.

C. The Meaning of "Libre Pratique" under the Treaty

In regard to relations among Member States the important question of which products are to benefit from the tariff and quota advantages mutually available in accordance with the Treaty required resolution. This question has been resolved by a Treaty provision according to which the benefiting products shall be:

1) those originating in Member States,
2) those coming from third countries which are deemed to be in libre pratique in the Member States.

The Treaty declares that products in libre pratique are those products coming from third countries in regard to which, in any Member State, import formalities have been complied with, customs duties collected, and no total or partial drawbacks (rebates) granted.

The interpretation and the implementation of these provisions have created practical problems which the Commission must solve. To this end, the Commission introduced a certificate of libre

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27 See infra Part II, Subsection D.
28 Treaty art. 9.
29 Treaty art. 10.
pratique which must accompany all goods circulating among Member States and which are to benefit from the advantages of the Common Market. The certificate serves to indicate that:

1) the goods originated in one of the Member States; or

2) the goods have been imported from a third country, and that the Member State which first imported them has actually collected the usual customs duties in accordance with its tariff schedules; or

3) the goods in question were imported from a third country, but have been transformed or finished in a Member State, and that the appropriate custom duties on the constituent parts imported from third countries into the transforming Member State were collected either upon entry into the territory of the Member State, or, in certain cases, upon their leaving the transforming Member State destined for another Member State.

The principle is, therefore, that to be deemed free to circulate within the Community, a product must be free to circulate within one of the Member States. The customs duties on the product must have been collected in that Member State, and the product must not have benefited from customs drawbacks, as products so often do in Europe upon being exported. The product also must not have been admitted temporarily.

This apparently simple system nevertheless may cause difficulties until the common external tariff of the Community has been established. At the end of the transitional period all merchandise coming from abroad will pay the same duties, irrespective of its point of entry, whether this be one of the Benelux countries, Germany, Italy, or France. Meanwhile, however, as long as the common external tariff is not in force, merchandise coming from abroad will pay different duties depending on the country of entry into the Community. Therefore, exporters in third countries could bring their goods into the Community through that member of the Six which at a given moment applies the lowest tariffs vis-à-vis third countries, or the least restrictive quotas, thereby creating risks of trade diversion and diversion of other commercial activity within the Community.

In fact, however, these risks are limited by Community rules:

1) In the first place, the fact that drawbacks of customs duties are prohibited on a product which is imported by a Member State from a third country and re-exported, either in its original form or transformed, to another Member State, results in two duties being
paid on it—that of the first importing state, and that of the second importing state. This second customs duty is, it is true, lower than the duty which would have been levied on the product had it been directly imported from a third country to the second Member State. The difference is, however, minimal during the first years of the transitional period and it is, in the majority of cases, made up by the duty of the first importing country. It is even certain that, at the beginning of the transitional period, it will be worthwhile in many cases of products manufactured in one of the Member States, incorporating materials imported from a third country, not to ask for a certificate of *libre pratique*, but rather to request a drawback. 

This is all the more true since, on January 1, 1959, the Member States made, as to a great number of products, the first tariff reduction of 10% applicable to imports from non-member countries, and there are as yet no substantial tariff preferences extended by the Member States to each other. In order to make clear how this works take the following example: an importer of Member Country A buys $100 worth of raw material in a non-member country on which there is a 20% duty on entry into Member Country A; he therefore pays $20 import duty to Member Country A. With this raw material he manufactures a product of which the ultimate total cost is $300. He exports this product to Member Country B. On entry into B this finished product would have been subject to a duty of 30% before the Treaty went into effect. During the transitional period the manufacturer-exporter of country A has the choice, when he exports the finished product to country B, between two solutions:

(a) either not to request that the product be considered in “libre pratique,” to benefit in this case from the drawback of the duty collected on the raw material and to pay the full tariff (30%) on the finished product when it enters country B; or

(b) to demand a certificate of “libre pratique,” not to request a drawback of the duty paid on the raw material and to pay the preferential tariff of the Community on the finished product when it enters country B. Obviously this choice will be dictated by the desire to sell his product at the lowest possible price in Member Country B.

If the manufacturer-exporter chooses solution (a), he receives a drawback of the duty paid on the raw material of $20. His product therefore costs only $280, and this is the basis for the calculation of the duty owed upon entry of the finished product into Country B. The cost of the product upon being imported into Country B is therefore

\[
280 + \frac{280 \times 30}{100} = 364.
\]

If he chooses solution (b), he does not ask for a drawback, and the cost of the final product after it has been imported into Country B is

\[
300 + \frac{300 \times 30}{100} = 390.
\]

After the first tariff reduction of 10% pursuant to the Treaty the tariff in Member Country B on the finished product will be 27% instead of 30%. The product can therefore be brought into Country B at

\[
300 + \frac{300 \times 27}{100} = 381.
\]

Since this is a higher cost than that of solution (a) the manufacturer-exporter will still have no reason to ask for the benefit of a certificate of “libre pratique.”

After the second reduction of 10% the tariff of Country B will be 24%. The product can then be delivered in Country B for

\[
300 + \frac{300 \times 24}{100} = 372- \text{still higher than the cost of solution (a).}
\]

After the third reduction of 10%, however, the tariff of Country B will be 21% and the product can be delivered in Country B for: \(300 + \frac{300 \times 21}{100} = 363\).

Thus after the third tariff reduction, but only then, solution (b) will be more advantageous than solution (a).
Of course as the Member States reduce tariffs among themselves without making such reductions available to third countries, the difference between the tariff that one Member State will apply towards third countries and the tariff that it will apply to other Community countries will be increased to the point where it will be economically beneficial, despite the prohibition against drawbacks, to effect the diversions of traffic described.

2) In the second place, another factor which will compensate for these risks is the mechanism of the first stages of the establishment of the common external tariff. This mechanism 31 will reduce the differences in the external tariffs of the Member States, increasing the tariffs on imports from third countries of Member States with the lowest duties, and decreasing the corresponding tariffs in Community countries where they are highest. Combined with the drawback prohibition, this reduction of the differences among tariff rates towards third countries will abolish the possible profits which merchants could otherwise obtain by trade-flow diversions. The differences between intra-Community tariffs and Community country tariffs vis-à-vis third countries will, of course, increase as the Six grant each other progressively increasing tariff preferences during the transitional period.

3) Thirdly, in cases where, despite these factors, trade diversions occur which prejudice the interests of certain Member States, the Commission must take all necessary steps to eliminate them. 32 The nature of permissible Commission action is not defined by the Treaty, but the Treaty provides that such action should cause the least possible disturbance in the functioning of the Common Market and should take into account the necessity of advancing, whenever possible, the establishment of the common tariff. If these diversions of traffic occur as a result of the disparities between intra-Community tariffs and tariffs of Member States on goods from third countries, the best curative measure would logically be a more rapid establishment of the common external tariff.

Other measures are also conceivable, however. For instance, a Member State might refuse to consider a product in libre pratique which had been imported from a third country by another Member State. Such national measures would prove extremely serious because they would impose obstacles to the free circulation of goods within the Community. Some Member States, although they do not

31 See Part III of this chapter.

32 Treaty art. 115.
go so far, do, in fact, require for imported products, which may have originated in and been imported from a third country, a certificate of origin as well as a certificate of *libre pratique*. If this certificate of origin shows that the product in question does, in fact, come from a third country, the Member State reserves the right to refuse to grant to this product the quota and tariff advantages of the Treaty and the right to treat the product as if it had been imported directly from a non-Community country. Until now measures designed to achieve this kind of protection have generally not been directed against diversions of commercial traffic due to the differences in tariffs, but against diversions due to differences among quota policies vis-à-vis third countries. These measures are directed notably at commerce in goods finished in the Community but originating in non-Community low wage countries, countries with multiple exchange rates, or countries of which foreign commerce is a state monopoly (Japan, Uruguay, and the countries of the East). The particular industrial products affected are natural and fabricated textiles, photographic and movie equipment, and the like. In fact, taking into account the low prices at which such products are sold by the producing country, some Member Countries can protect their own industries only by recourse to a quota system or to an absolute prohibition of imports. If such products could enter under cover of a certificate of *libre pratique* issued by another Member State whose import policy is less restrictive with regard to third countries, the more restrictive policies of the first country would be frustrated. Finally, and again with a view to avoiding diversions of traffic, the Commission envisages the imposition of advance charges in lieu of customs duties on products originating in third countries when they pass from one Member State into another Member State, but there is as yet little information available in this regard.

The free circulation of goods within the Community will remain a serious problem so long as the common external tariff of the Community is not in force and the countries of the Community have not adopted a common quota policy towards third countries. In order to avoid the rather complex formalities, which could obstruct intra-Community trade, the drafters of the Treaty refused to provide a means for checking on the origins of goods. Protectionist reflexes are quasi-automatic, however, and ultimately the certificate of origin will reappear in acute cases. Community countries will no doubt be forced to make considerable efforts to rid themselves effectively of red-tape and of the useless nuisances which, either by force of habit
or under the pressure of protectionists, national governments tend to multiply.

D. CLAUSES PROVIDING SAFEGUARDS AGAINST DIFFICULTIES RESULTING FROM THE ELIMINATION OF QUOTAS

The Treaty provides safeguard clauses permitting a Member State, when difficulties arise, to take protective measures with a view to limiting the volume of its imports. These are:

1) a clause which may be invoked in case of balance-of-payments difficulties; and

2) a clause which may be invoked in case of special difficulties in a given sector of its economy.

I. THE CLAUSE PROVIDING SAFEGUARDS AGAINST BALANCE-OF-PAYMENTS DIFFICULTIES

The clause concerning balance of payments is similar to the usual clauses included in all international trade agreements. To prevent Member States from invoking it too often, however, the Treaty imposes very strict conditions on its applicability.

In the first place, the Treaty envisages a procedure which is, in a sense, preventive. The economic, financial, and monetary policies of each Member State are kept under constant review in order to avoid disequilibriums in the balance of payments. Each Member State must therefore pursue economic policies which will ensure equilibrium of its over-all balance of payments, maintain confidence in its currency, and at the same time ensure a high level of employment and stable price levels. In order to facilitate the attainment of these objectives, the Member States are to coordinate their economic and monetary policies. The institutions of the Community, and notably the Commission, a special consultative committee, and the Monetary Committee are to formulate opinions for the Member States concerning the policies which they should follow to assure normal functioning of their economies as well as of the economy of the Community as a whole. Obviously constant supervision of the evolution of the economy and of financial, economic, and monetary policies constitutes the best means of avoiding disequilibriums.

Secondly, if despite supervision and coordination of current policies of the Member States, disequilibrium in balances of payments occur, the consultations for which the Treaty provides must take place. The Treaty describes disequilibrium as difficulties or serious threats

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83 Treaty arts. 103–105.
of difficulties as regards a Member State's balance of payments resulting either from an “over-all disequilibrium of the balance of payments or of the kinds of currency at its disposal and where such difficulties are likely, in particular, to prejudice the functioning of the Common Market or the progressive establishment of the common commercial policy. . . .” 34 The Treaty takes into account, then, such disequilibriums as might constitute a threat for the internal functioning of the Common Market—that is, which might impel a country to re-establish protective measures with regard to imports originating in other Member States—or a threat to the common commercial policy—that is, which might bring a Member State to follow, in regard to third countries, a different policy than that of other Community countries. An accentuation of policy differences in regard to third countries would in fact create the risk of larger trade diversions and, as a consequence, of reinforcement of controls on the circulation of goods among Member States.

The procedures contemplated in these cases do not permit the country in question to re-establish protective measures in regard to imports. The Treaty provides that the Commission shall, without delay, proceed to an examination of the situation of the country in question, as well as of the measures that country has taken or may take in order to bring its economy into balance. The Commission shall make recommendations with these ends in mind. Even though the Treaty does not say so explicitly, it is clear that at this stage the recommendations of the Commission are to be directed at reform of the internal economic and financial policies of the country involved (reduction of public expenses, reduction of credit to private enterprises, increase of taxes, higher discount rates or, even, monetary revaluation) but not at the direct or quantitative control of its imports.

The procedure contemplates that, if these measures prove inadequate, the Commission thereafter shall recommend to the Council that it institute the mutual assistance measures for which the Treaty provides, subject to a majority vote of the Council. The essence of the notion of mutual assistance is its Community character. Mutual assistance signifies that the associated countries of a country in difficulties are obliged to aid it in overcoming them, thereby emphasizing the interdependence of the Six.

The Treaty contemplates that mutual assistance may take the following forms:

1) Concerted action within such international organizations as

34 Treaty art. 108.
may be asked for help by the countries of the Community—that is, within those organizations which can grant credits in foreign currencies to the country in difficulty.

2) Action to avoid trade diversions when the country in difficulties maintains or re-establishes quotas on goods imported from third countries. The country in difficulties will not always be authorized at this stage to re-establish restrictions vis-à-vis other Community countries, although it can vis-à-vis third countries. The aim of such restrictions may well be defeated, however, if other Member States continue unrestricted importation from third countries of the products subjected to quotas by the country in difficulties, since the entry of such products, accompanied by a certificate of libre pratique from another Member State cannot be restricted. Because this is true, the other Member States must, in such cases, take the necessary steps to prevent the products in question from being re-exported to the Member State which finds itself in difficulties.

3) The grant of credits by other Member States, if they agree this is indicated.

4) Finally, and during the transitional period, a recommendation by the Commission to the other Member States to reduce tariffs more rapidly or effect larger quota increases in order to facilitate the increase of exports from the country in difficulties to them, thereby permitting it to increase its foreign exchange receipts.

If mutual assistance recommended by the Commission is not granted by the Council, or if mutual assistance is granted but the measures taken are insufficient to mitigate the difficulties of the country concerned, the Commission is to authorize the country in difficulties to take protective action with regard to exports of the other Community countries. The Commission must define the conditions applicable to such measures, their timing and the like, but the Treaty does not indicate the form which they are to take. It is likely, however, that, during the transitional period, they may, for example, delay the elimination of obstacles to trade (i.e., of tariffs and quotas) or even reverse the process, and that they might, before anything else, introduce quantitative restrictions on imports during the decisive period.

The process thus described is obviously quite long and complex. The Treaty expressly provides that the country in difficulties may initiate no protective measures without prior authorization of the Commission. The time required for the Commission to intervene
may be unduly long if a sudden crisis in the balance of payments occurs, however. In this case the Member State concerned may take the necessary steps without preliminary authorization—but purely to prevent the situation from deteriorating. The Treaty provides that these steps shall cause the least possible disturbance in the functioning of the Common Market and shall not be more extensive than is absolutely indispensable in order to remedy the sudden difficulties which have arisen. Even after these steps have been taken, the Commission may recommend that the Council grant mutual assistance, which in turn may lead the country in difficulties to suspend its own protective measures. In this regard the Treaty provides that by majority approval of an opinion of the Commission the Council may require the country in difficulties to modify, suspend, or abolish its safeguard measures.

The safeguard against continuing balance-of-payments difficulties may be invoked during or after the transitional period. Because of the interpenetration of the economies of the Member States—which will be increasingly significant as the transitional period expires—and because of ever closer economic, financial, and monetary cooperation, the likelihood that balance-of-payments crises will be Community-wide rather than national in scope will approach inevitability.

2. THE CLAUSE PROVIDING SAFEGUARDS AGAINST DIFFICULTIES IN PARTICULAR SECTORS OF THE NATIONAL ECONOMIES

The safeguards against difficulties in particular areas of economic activity are only applicable during the transitional period. The reason for this is that during this period the progressive abolition of obstacles to trade and the resultant competition among economic activities of the various Member States may create “serious difficulties which are likely to persist in . . . [a] sector of economic activity or difficulties which may seriously impair the economic situation . . . [of a] region.” Such difficulties might manifest themselves by a decrease in the activity of enterprises in a given sector of the economy, by unemployment, or by substantial economic stagnation or retrogression of a given region.

Obvious problems result, but it is also obvious that recourse to safeguards must be viewed with a certain reserve. No government
may remain unmoved in the face of a deteriorating situation in a sector of its economy or of a depression in a region of the country, especially where either seems to be caused by foreign competition. If it took no action, the public reaction would be violent. But, on the other hand, if the goal of the Common Market is better distribution of labor among the Six, and the elimination of uneconomic activity in one country in favor of more efficient activity in another (and thereby, the attainment of a higher level of productivity for the Common Market as a whole), then it is inevitable that certain enterprises will disappear in some countries because they are subject to economic, financial, technical, geographical, or natural conditions which prevent them from meeting the competition of enterprises capable of increasing productivity. A balance is, then, to be sought, which will permit progressive elimination throughout the Common Market of inefficient enterprises, and will, at the same time, avoid violent economic disruptions which could provoke serious social or even political crises.

The entire structure of the Treaty was, moreover, determined by the need to maintain this balance as is indicated by:

1) the duration of the transitional period,
2) the flexibility of the program of progressive abolition of tariffs and quotas among Member States,
3) the provisions relative to the harmonization of legislation,
4) the creation of the European Investment Bank, and
5) the creation of the European Social Fund.

It is evident, however, that implementation of the Treaty is conditioned, not only on these provisions, but also, and above all, on economic stability and a continually developing prosperity both in Europe and throughout the world. Only under these conditions can the Community countries accept the disappearance of some of their enterprises for it is only under such conditions that their highly-developed economic structures will be flexible enough to permit the people affected to re-establish themselves in other pursuits without too much difficulty.

Nevertheless, a safeguard clause remains necessary where, in spite of the flexibility of the provisions of the Treaty and the steps which each country is obligated to take to adapt itself in order to allow enterprises in their turn to adjust themselves to foreign competition, a grave crisis develops. For the reasons already indicated, recourse to this clause is, however, strictly regulated.

The government concerned may not invoke this safeguard clause
unilaterally, but must request authorization from the Commission, and its purpose must be to "restore the situation and adapt the sector concerned to the Common Market economy." Moreover, the Commission itself must determine the measures of safeguard which it deems necessary, stating precisely the conditions, the means, and the duration of their application. These measures, and their duration, may be only such as are absolutely necessary to permit restoration of the situation. Finally, the Treaty provides that priority should be given in the choice of measures to those which will least disturb the functioning of the Common Market.

The Treaty does not specify the measures which the Commission may decide to authorize, but leaves the Commission absolutely free to determine them. Nevertheless, it seems entirely likely that, in the case of activities which—once reorganized—give every indication that they will be able to survive, the Commission will elect measures which will both assure that the reorganization will take place as rapidly as possible and will afford the activity more and longer-lasting protection. Thus protected, the reorganization will take place—perhaps with the aid of subsidies or of the continuation of quotas or tariffs on the importation of the products concerned or other such aids. If, however, the activities concerned ought to disappear because, for one reason or another, it is impossible to improve their productivity sufficiently to make them reasonably profitable, the Commission will probably elect measures permitting as gradual a disappearance as possible. At the same time, of course, steps must be taken to find employment for workers losing jobs and to develop in the region in question economic activity better adapted to the conditions obtaining.

III. THE RELATIONS OF THE SIX WITH THIRD COUNTRIES

The problem of the relations of the Community with the rest of the world are of extreme importance to both. The Community is, after all, the world's second largest commercial power (in 1957, the U.S. share of world trade was 17.6%, that of the Community 17.4%, and that of the United Kingdom 11.2%); and yet this vital problem is far from solved. The Treaty creates some rules directed at the Community relationship with third countries, but it leaves a great number of questions to be resolved during the transitional period by an interplay of the various political and economic forces
which will confront each other both within the Community and without it.

The most debated question today is whether the Community will be turned in upon itself or outwardly oriented—that is, whether the Community will develop a protectionist or liberal commercial character. No attempt to answer that question will be made in this chapter. At this juncture one can only describe the context within which this question arises—that is, describe the Treaty rules regarding the tariff and foreign commercial policies of the Community, the way they have been applied to date, and the place of the Community in the European and world setting, taking into account the factors which, for the last two years, have influenced its relations with the rest of the world (the free trade area and the Dillon proposals).

A. THE ESTABLISHMENT OF THE COMMON EXTERNAL TARIFF

I. METHODS OF DETERMINING THE TARIFF

The General Agreement on Tariffs and Trade, of which the Six are members, excepts customs unions in applying the most-favored-nation principle to tariffs.37 In order to qualify for this exception, a customs union must conform to a certain number of conditions fixed by the G.A.T.T., however. One condition is that the incidence of the external tariff of the union should not, taken as a whole, be greater than that of the national tariffs replaced.

By virtue of this condition, the Treaty, as a general rule, envisaged a tariff corresponding roughly to the arithmetical average of the tariffs of the four constituent customs territories.38 (Luxembourg, the Netherlands, and Belgium, having for the last ten years been part of a customs union, are considered as a single customs territory.)

The question of whether or not the arithmetical average of the tariffs of the four territories conforms to the rules of G.A.T.T. has long been debated. Within as well as outside the Community, it has been argued that a weighted average which would take into account not only the present level of tariffs of each of the four territories, but also the value of goods imported by these territories would more nearly conform to the spirit of G.A.T.T. Those in favor of this thesis calculate that on the basis of a weighted average the external

37 See Introduction at note 3 supra.
38 Treaty art. 19.
tariff of the Community would be, on the whole, lower than that resulting from the arithmetical average, given the fact that the two largest importers of the Community, Germany and the Benelux countries, are also the territories with the lowest tariffs. This would, of course, be true only of the external tariff viewed as a whole, since as to certain products a tariff based on a weighted average would be higher than one based on the arithmetical average. Discussions in G.A.T.T. of the choice between the two methods of averaging have not yet resulted in a decision.

As in the case of the abolition of tariffs among countries of the Community, January 1, 1957, was chosen as the date for determination of the tariff levels to which the Treaty rules would apply. 39

Italy, however, has for the last ten years or so, in fact, applied a tariff which is generally 10% lower than the tariff for which her laws provide. The Treaty provides that in calculating the arithmetical average, the legal tariff (consequently the higher of the two) is to be used.

Although they adopted the arithmetical average in principle, the drafters of the Treaty also wished to establish certain ceilings on the results which the calculation of such an average could produce. The Treaty therefore provides that the common external tariff shall not exceed:

1) 3% on some products of which the most important among industrial products are: iron pyrites, raw graphite, calcium phosphate, flax, arsenic sulphur, natural gas, tar, bitumen, sodium nitrate, raw rubber, raw furs, wools, wool linters, combed cotton, cotton linters, etc. (List B).

2) 10% on other products of which the most important among the industrial products are: glycerine, resin, petroleum bitumen, tannins, coloring matters of vegetable origin, essential oils, liquid resin, colophene; sheets and leaves of natural or synthetic rubber; leather and hides of cattle, sheep, and goats; newsprint in rolls, wool yarn (not yet finished for retail sale), linen, ramie, hemp, cotton, jute; iron and steel, iron bars and sheets, sheet iron, iron wire; bars, sections, and wire of brass, nickel, aluminum, lead, and zinc (List C).

3) 15% on other products of which the most important among industrial products are: alkaline metals, mercury, ammonia, zinc oxide (List D).

4) 25% on another list of products of which the industrials are;

39 Ibid.
organic chemical products, synthetic organic coloring matter, artificial plastics, with the exception of products manufactured from plastic (List E). It should be added, however, that where, on January 1, 1957, the Benelux countries applied to the respective products a duty lower than 3%, this duty is, according to the Treaty, to be raised to 12% in calculating the arithmetical average. The result is plainly an attempt—at the same time that a ceiling of 25% on the external tariff of the Community is fixed—to avoid establishing too low a tariff on these products by increasing the amounts upon which the calculation of the average is based.

On the other hand, for specified products the Treaty fixes a list of duties which France must take into consideration in calculating the arithmetical average. These duties are higher than those in fact applied by France on January 1, 1957 (List A).

With regard to other products, the common tariff is fixed by the Treaty itself (List F), and is, in some instances lower, and in others higher, than the duty which would have been obtained had the arithmetical average been calculated. List F products are predominantly agricultural, but some are industrial, such as phosphorus, iron-oxides, sheets of veneer, and veneered panels, on all of which the tariff will be high, and some basic textiles (cotton, hemp, jute) and minerals (brass, zinc) on which Community tariff will be non-existent.

Finally, the Community tariff on a last category of products will not be determined according to the arithmetical average, but by negotiation among the Member States. These products are found in the much-discussed list G.40

2. MEANS OF IMPLEMENTATION OF THE PROVISIONS CONCERNING THE COMMON EXTERNAL TARIFF

Once the Community tariff is determined, Member States must progressively put it into effect. Since in toto it corresponds to the arithmetical average of the tariffs in force on January 1, 1957, in the four customs territories of the Community, some countries will have to increase, and others to decrease, duties in order to arrive at the common tariff. These changes are to be made during the transitional period so that at its end the common tariff will be in force. They are not to be initiated, however, until December 31, 1961, a

40 See text of this Part III, Section A at Subsection 4.
date which, absent extension of the first stage, will also mark the end of that stage. At that time Member States must, in cases where the duties applied on January 1, 1957, differed no more than 15% in either direction from the common tariff, put the common tariff into effect. Each Member State will have fulfilled its entire Treaty obligation as far as products thereby affected are concerned. In respect to products on which the difference in either direction is greater than 15%, the state in question must, on December 31, 1961, reduce this difference by 30%. A second reduction of 30% of the difference is to be made at the end of the second stage.

The Treaty does not indicate when and how the difference still existing after the second reduction is to be eliminated. It specifies, however, that the common tariff is to be in force in its entirety at the end of the transitional period, which means that each country must, one way or another, eliminate during the third stage the remaining differences.

An example with figures makes it easier to understand how the system works. Given a product to which the Benelux countries applied (on January 1, 1957) an import duty of 11%, Germany a duty of 17%, France a duty of 23%, and Italy a duty of 29%, the arithmetical average would be: \( \frac{11 + 17 + 23 + 29}{4} = 20\% \). Since the German and French duties of 17 and 23% respectively differ by 15% from the common tariff of 20%, Germany and France will put the common tariff into effect on December 31, 1961. The Benelux countries, on the other hand, will reduce by 30% the difference between the 11% duty in effect on January 1, 1957, and the 20% common tariff. The Benelux duty will therefore become 14%. By virtue of the same rule, Italy will reduce her duty to 26%. At the end of the second stage Benelux will raise its duty to 17%, and Italy will reduce hers to 23%. In the course of the third stage, both Benelux and Italy will attain the 20% rate.

The Treaty also provides for the case where some duties of the common tariff—those which have to be negotiated by the Member States (List G)—are still unknown at the end of the first stage of the transitional period. In this case the rules described above are to be applied six months after the date these duties are established.

41 Treaty art. 23. In the spring of 1960 the feasibility of advancing the Dec. 31, 1961, date was, however, being discussed. See also Chapter I supra.

42 Treaty art. 20.
The Treaty also provides that the Member States shall be free, in order to align their duties with the common customs tariff, to modify these duties more rapidly than indicated above.\textsuperscript{43}

3. TECHNICAL PROBLEMS OF IMPLEMENTATION OF THE RULES ESTABLISHING THE EXTERNAL TARIFF

If the Member States are to adopt duties which conform with the external common tariff, they must, of course, know the amount of the latter. The determination of this tariff raises a great number of technical problems, however, and the Treaty is of little help in resolving them. The Commission is to suggest solutions to the Council \textsuperscript{44} and reference must therefore be made to the work of the Commission since the Treaty went into effect to know the context within which these problems are to be progressively solved.

In the first place, a comparison of national tariff schedules must be made in order to define the bases upon which the arithmetical average is to be calculated. Present schedules, in fact, differ from one another. For instance, in one schedule duties are levied on cars in accordance with their weight, whereas in another the number of cylinders is determinative. One of the first tasks therefore was the juxtaposition of the various customs headings of the four tariffs of the Community: the result was the elaboration of a list comprising 20,000 headings, whereas an average tariff list rarely includes more than 5,000.

In the second place, a single tariff schedule must be established for the Community which will give a basis upon which the common tariff can be established. This schedule should normally comprise about 5,000 headings. Obviously this will entail choices, in the sense that, to return to the example cited above, it must be decided whether for passenger cars tariffs are to be calculated according to weight or according to the number of cylinders.

Thirdly, a "table of concordance" between the headings of the Community schedule and those of the national schedules must be created. Such a table will make calculation of the arithmetical average possible and, at the same time, will provide a basis for determination of the tariffs which each Member State will have to increase or decrease in the course of the successive stages of tariff equalization. Determination of these tariffs obviously raises another delicate

\textsuperscript{43} Treaty art. 24.

\textsuperscript{44} Treaty art. 21.
technical problem, since certain Member States levy an *ad valorem*, and others a specific,\(^45\) duty on the same product.

However, the calculation of the arithmetical average under these conditions may bring to light internal disequilibriums in national tariff structures. Indeed, a rational tariff structure should provide higher and higher tariffs on goods as they are subjected, beginning with the raw material, to progressively greater degrees of transformation. For example, there should be a progression in the amount of duties levied on raw wool, carded wool, wool yarn, wool cloth, and wool clothing. Application of the arithmetical average could, as far as the common external tariff is concerned, result, however, in the application of a duty to wool yarn which is lower than that applicable to carded wool. An equilibrium must therefore be established within tariff schedules which will take account of the degree to which various goods have been finished.

The work begun with this end in view almost two years ago by groups of customs experts was virtually completed by the beginning of 1960. It was, in fact, indispensable that the tariff of the Community be known by this time to permit G.A.T.T. tariff negotiations to begin.\(^46\)

4. **LIST G: EXTERNAL TARIFF ITEMS YET TO BE NEGOTIATED AMONG THE SIX**

In the course of the Treaty negotiations, it was impossible for the Member States to agree on the application of the rule of the arithmetical average, or on a maximum ceiling, or on a common duty with regard to several products. These products are enumerated in list G which was annexed to the Treaty. This list includes, most importantly, raw materials on which certain countries of the Community levy very high duties and others very low ones. Those states which apply high duties do so because the cost of their national production is in general much higher than the average world price. If a lower duty were put in effect, these countries would have to cease production, since they are unable to produce competitively. Serious economic, financial, and above all, social consequences would result. But should the external tariff of the Community be fixed at the level of the higher tariffs, the transforming industries of those countries

\(^45\) A specific duty is one which takes into account the nature only and not the value of the product imported: for example, regardless of its value a given raw material is subjected to a duty of $1 per pound or a given electrical appliance to a duty of $1 per appliance.

\(^46\) See text of this Part III, Section E at Subsection 5.
which levy a low, or even no, duty would be forced to procure the raw materials affected at a higher price than the present—that is, the world market—price. Their ability to compete in the sale on world markets of goods manufactured from these raw materials would be correspondingly diminished.

The conflict among the Member States concerning list G exemplifies a more general problem which the Community as a whole faces. If the Community is to be a world commercial power, capable of exporting at competitive prices, its industries must procure raw materials at the most advantageous prices, which is to say, at world market prices. If these prices are to be increased by heavy duties, the export position of the interested industries will be worsened. If, on the other hand, the Community protects the raw materials it produces with high tariffs, it will encourage their exploitation even though they can only be sold at higher than world prices, and it will run the risk of developing tendencies toward autarky.

Because the products in list G are, with regard to the determination of the common external tariff, subject to a special procedure, special Treaty rules were provided for them. The Treaty provides that the Commission shall take the appropriate steps to ensure that negotiations among the Member States will be undertaken before the end of 1959, and concluded before the end of 1961 (that is, before the initiation of the first changes in the tariffs of the Member States directed at the establishment of the common external tariff). If, however, in the case of any product no agreement has been reached by that date, the Commission is to submit proposals to the Council recommending the duty to be levied. The Council is to accept or reject the proposals of the Commission by means of a unanimous vote during the second stage, and by means of a majority vote during the third stage.

In any case, duties on products in list G must be determined by the end of the transition period at the latest. If problems are then still outstanding, political decisions will obviously be necessary to resolve them. The conclusion seems justified even now that the requisite compromises will, in one way or another, be achieved.

Consequently, as long as the customs duties of list G were unknown, the Member States could take no steps to reduce differences among the tariffs that each levied on these products—which, by definition, varied greatly from one another. For this reason they created the greatest risks that trade diversions would occur. On the
other hand, since these products are generally of considerable importance in world commerce, and since some third countries have a vital interest in exporting them, the uncertainty was particularly resented. This explains the lively criticism of list G within G.A.T.T. Finally, the lack of information on list G tariffs complicated the G.A.T.T. tariff negotiations initiated pursuant to the Dillon proposal.\footnote{See note 46 \textit{supra}.}

Because of these several difficulties the Commission did not wait until the end of 1959 to bring pressure on the Member States to begin negotiations. As a result of the Commission's initiative, negotiations were in fact begun at the beginning of 1959. Working groups composed of the representatives of the Commission and of the governments of the Member States have met together on several occasions. Discussions of these groups involved—it may be added—a profound examination of the situation of each product on the list: production, imports, exports, prices, capital invested in the producing enterprises of the Community, labor expended, perspectives of development, possibilities for the increase of productivity, and the like. Ultimately, in March, 1960, the Six reached agreement on the tariffs of list G (with the exception of those on petroleum products). Their successful compromises in this sensitive area indicate their political determination to proceed with the establishment of the Common Market.

B. The Liberalization of Trade with Third Countries

Strictly speaking the Treaty imposes no precise obligations on the Member States concerning quotas on imports from third countries. It merely indicates in general terms that the Member States shall coordinate their commercial relations with third countries in such a way as to bring into existence, not later than the expiration of the transitional period, the conditions necessary for the implementation of a common policy with regard to foreign commerce.\footnote{Treaty art. 111.} It adds that the Commission shall submit to the Council proposals regarding the procedure to be followed in the course of the transitional period to coordinate action, and to achieve a uniform commercial policy. The Council shall accept these proposals by unanimous vote during the two first stages of the transitional period, and thereafter by majority vote. Finally, the Treaty establishes, as a goal for the
Member States, uniform lists of third-country products not subject to quotas which are as inclusive as possible. To further this aim the Commission shall make appropriate recommendations to them.

The relative vagueness of these provisions, if compared with those which regulate the relations among the Member States and those relative to the common external tariff, may seem astonishing. It has in fact both legal and factual justification.

One fact which justifies this vagueness is the extraordinary complexity of the problem. The points of departure of the Member States were, in fact, very different when the E.E.C. Treaty was negotiated. On the one hand, the lists of liberated third-country products of each Member State differed among themselves and still differ. Germany's lists of liberated products imported from her partners in the O.E.E.C. differ from those of products imported from countries which belong neither to O.E.E.C. zone nor to the dollar area. Italy has different lists for these areas, but, in addition, has lists in regard to products of countries which belong neither to the O.E.E.C. nor to the dollar area which differ among themselves. Moreover the differences in these lists in regard to a given area are differences in scope as well as of composition. The situations are even more disparate in regard to the relations between each of the Six and those countries which do not belong either to the dollar area or to the area of the O.E.E.C.—and this remark relates only to over-all percentages. If one examines the lists of products, a comparison becomes practically impossible.

Firm obligations to unify lists of liberated products would create inextricable problems from a practical standpoint and have grave consequences with regard to commercial policy. In fact, if these lists were harmonized on the basis of the lowest common denominator, some Member Countries would be forced to retrogress and to re-establish quotas on a great number of products. They are not prepared to do so, and moreover, as will be clear from the following discussion, to do so would be to violate international obligations imposed by O.E.E.C. and the G.A.T.T. If the lists were harmonized at the most liberal level, some Member Countries would be forced to make efforts which, either because of their balances of payments, or for reasons of national commercial policy, they are not in position to make immediately or soon. If the mean between the two were chosen, it would be practically impossible to determine it. Each Member State has, moreover, bilateral commercial agreements with
most third countries in each area, fixing quotas on the imports of goods from them. In exchange for the import concessions involved, these third countries grant concessions in regard to Member State exports. The counter concessions obviously are different for the various Member States and also vary according to the third country granting them. If the lists of Member States of liberated products from third countries were made uniform, coordination of the bilateral negotiations between the Six on the one hand and each of the third countries on the other should be a consequence. This would create complex problems which neither the Member States nor the third countries are now prepared to face. One of the avowed objectives of the Community is, of course, to achieve complete uniformity at the end of the transitional period. But the fact remains that it was not possible to write into the Treaty specific obligations of the Member States as to the steps to be taken in this direction during the transitional period.

To these factual considerations must be added legal ones. The Six are members of the International Monetary Fund (I.M.F.) of G.A.T.T. and of the O.E.E.C. Each of these international organizations has rules regarding quotas on commercial imports which increase the difficulties of achieving uniform lists of liberated products—at least as things stand at present. G.A.T.T. is an international agreement to which approximately forty countries are parties and which has as its object the creation of something like a code of good conduct in international commercial relations and thereby a world as free of obstacles to trade as possible. Based on national-treatment and most-favored-nation clauses, G.A.T.T. hopes to achieve its ends by outright prohibition of import quotas (except in cases of balance-of-payments difficulties) and by the reduction of tariff barriers through negotiation.

Sixty-eight nations participate in the International Monetary Fund. Its purpose is to make possible the liberation of financial transactions on a world-wide and non-discriminatory basis and to create a better equilibrium of international financial relations, specifically by means of realistic exchange rates. It has important resources at its disposal to aid countries suffering from temporary balance-of-payments difficulties. Because these difficulties are often due to the internal management of the finances of member countries, it also has certain powers of inspection and recommendation.

These two organizations were created at the end of the last war. Because of reconstruction needs and the situation which obtained
generally at the time of their creation—which made it impossible to apply their rules without reservation—these rules were to become effective only gradually during periods of transition. The time is now coming when the end of these transition periods can be foreseen.

O.E.E.C. imposes upon its members a level of liberalization at least equal to 90% of their 1948 intra-European imports. At the time the Rome Treaty was negotiated, all Member States, with the exception of France, had effectively reached, and even largely surpassed, this level. But France was far from doing so. Indeed, after the Treaty was signed difficulties in her balance of payments forced France (in June, 1958) to re-establish quotas on all imports. Thus, even if France—pointing to her difficulties and invoking the safeguard clause provided for this purpose by the rules of the O.E.E.C.—could suspend liberalization within the O.E.E.C., other Community countries, having no balance-of-payments difficulties, could not have invoked the same clause for the same purpose even if they had wished to do so. In December 1958, on the eve of the effective date (January 1, 1959) of the first measures affecting commerce contemplated by the Treaty, France had—as to O.E.E.C. countries—achieved the 90% level. Since then she has gone even further, and has now reached 94%. Since each country is, according to O.E.E.C. rules, free to choose the products on which it abolishes quotas (provided it attains the obligatory percentages) the lists of liberated products within O.E.E.C. of the respective Common Market countries differ from one another, to the point that unification of these lists would:

1) either force certain Member States to re-establish quotas on certain products and to fall below the 90% liberalization level without being able to invoke the safeguard clause to justify this regression; or

2) force other Member States to liberalize immediately certain products within the O.E.E.C.—which they are not now ready to do. Because, moreover, immediate liberation of these products would in their opinion create serious difficulties, even within the Community, the Treaty drafters established the rules for a progressive increase in quotas.50

In relation to the G.A.T.T., the question is even more delicate, and its present development particularly interesting. The G.A.T.T. prohibits absolutely quantitative restrictions on imports, recognizing only tariffs as legitimate means of protection. This is its basic

50 See Part II supra.
principle, and only one exception is recognized: difficulties in balances of payments. Moreover, the G.A.T.T. categorically affirms the principle of non-discrimination in the administration of quantitative restrictions maintained or newly established by a country which is suffering from balance-of-payments difficulties. It recognized derogations from this principle only to the extent that the International Monetary Fund also permits differences in treatment with regard to the restrictions on foreign exchange.

In the post-war years, G.A.T.T. applied these two principles with a great deal of flexibility. Because of their reconstruction and development needs, most of the European countries had balance-of-payments difficulties. Moreover, because of the absolute separation introduced before, during, and after the war among the monetary systems of countries, and the fact that transactions were effected according to bilateral agreements—in short, because of non-transferability among currencies—G.A.T.T. accepted the maintenance of quantitative restrictions and their discriminatory application. It even went so far as to close its eyes to the intra-European liberalization which the O.E.E.C. had introduced among its members, and which was in essence discriminatory in regard to the other contracting parties to the G.A.T.T. since the O.E.E.C. countries abolished quotas among themselves without according, necessarily, the same treatment to other G.A.T.T. members. This tolerance on G.A.T.T.'s part was obviously motivated by the fact that the O.E.E.C. countries had made their currencies transferable among themselves by virtue of the creation of the European Payments Union, which also comprised a system of automatic credits among its members.

However, as balances of payments of the countries of Europe improved, G.A.T.T. exercised an increasing pressure on them to liberalize their imports with respect to countries outside Europe. Indeed, the O.E.E.C. had itself contributed to this geographical extension of liberalization by urging its members to abolish quotas on their imports, notably those from Canada and the United States. With the disappearance of the European Payments Union, and the advent of external convertibility of most European currencies in December 1958, the pressure of the G.A.T.T. and of the International Monetary Fund for integral and non-discriminatory liberalization strongly increased.

The result of the liberalization of their imports on a worldwide scale, which is gradually being achieved by the Six, is that the practical difficulties of a common quota policy are becoming greater and
greater. In fact, although the G.A.T.T. envisages the possibility that a customs union may create a preferential tariff system among its members, it apparently envisages nothing of the kind concerning quotas. The result is that, as things now stand, each country of the Community (as is true of the other countries of G.A.T.T.) is examined individually by the International Monetary Fund and G.A.T.T., and is encouraged to liberalize its imports towards all of the other countries of G.A.T.T. and of the International Monetary Fund, in accordance with the state of its individual balance of payments. Since the decisions of G.A.T.T. are directed at individual countries, it may be that it will consider that one country of the Community should free all of its imports vis-à-vis the rest of the world but that another is justified in maintaining certain quotas provisionally—with the understanding that in conformity with the basic principle of the G.A.T.T. and the Monetary Fund, it must administer these quotas in a non-discriminatory manner as to all G.A.T.T. and I.M.F. members. This means that no preferential treatment shall be accorded to Community members.

The legal and factual elements of the common-quota-policy problem which deserve emphasis are:

1) the virtual impossibility of establishing a common policy of the Member States in regard to import restrictions, the only point on which, theoretically, coordination may be achieved in conformity with the obligations of these countries to G.A.T.T. and I.M.F. being a complete liberalization of imports from all G.A.T.T. and I.M.F. members;

2) the gradual desuetude of those rules of the Treaty which relate to the progressive increase of quotas among the Member States of the Community. It is evident that if, under the pressure of non-member states united within G.A.T.T. and the Monetary Fund, each Member State is led to abolish import quotas on industrial products originating in G.A.T.T. and I.M.F. countries, the complex rules of the Treaty concerning the progressive relaxation of quotas among its Members will lose their justification. Naturally, each country of the Community, in removing quotas on imports from G.A.T.T. countries, will also remove them on goods from Community Countries, because Community Countries are members of G.A.T.T., and because the Treaty provides in Article 111 that, “if Member States abolish or reduce quantitative restrictions in regard to third countries, they . . . shall accord identical treatment to the other Member States.”

This is the current legal and factual context of the problem of
liberalization vis-à-vis the rest of the world of the imports of Member States. Three additional comments are appropriate.

1) The legal situation described applies to the relations between the Member States of the Community and the countries of the O.E.E.C. and G.A.T.T. It does not apply to relations with those countries which do not belong to these organizations, meaning, largely, the countries behind the Iron Curtain.

2) The situation has also been described on the assumption that in the years to come it will in fact be possible to apply in full the rules of G.A.T.T. and of the Monetary Fund. 51

3) Safeguard clauses must also be considered.

C. SAFEGUARD CLAUSES

There are, strictly speaking, no safeguard clauses in the Treaty which relate specifically to the establishment of an external tariff and lists of liberated goods. The sole provision of any relevance is Article 26 of the Treaty, which provides: "The Commission may authorize any Member State encountering special difficulties to postpone the lowering or the raising, in accordance with the provisions of Article 23, of the duties on certain headings of its tariff." But the freedom of the Commission in this connection is limited by what follows in Article 26: "Such authorization may only be granted for a limited period and for tariff headings which together represent for such State not more than five percent of the value of its total imports coming from third countries in the course of the latest year for which statistical data are available." Obviously these provisions could come into play if one of the Member States should encounter difficulties in lowering a customs duty vis-à-vis third countries which, initially, was higher than the future common external tariff. These difficulties might result from the fact that some third country was in a particularly strong competitive position with regard to a product to which that duty was applicable. But if the Member State's domestic industry cannot withstand the competition of third-country industries—even with continued customs protection—there is every chance that it is not in a position to withstand the competition of the corresponding industries of other Member States whose products will not, ultimately, have to cross customs barriers. Recourse to Article 26 is therefore more or less tied to recourse to Article 226. 52

51 At the moment, this is disputed, and the underlying theory of the work pursued within the Community for the elaboration of a common external commercial policy assumes non-application of G.A.T.T. rules.

52 See text at note 36 supra.
But the most interesting problem is the one which balance-of-payments difficulties of a Member State could create, given the obligations of that state to the Monetary Fund and G.A.T.T. One aim of the rules of the Treaty is to avoid, or failing that, to delay as long as possible, situations in which one Member State will be forced, by balance-of-payments difficulties, to adopt protective measures in regard to its imports from Community countries. The first action envisaged for the Community will, it is true, be designed to allow the country in question to maintain as liberal an import policy, vis-à-vis non-Community countries, as possible. Specifically, the first measure envisaged consists in concerted action with those international organizations to which Member States may have recourse. Should one of these organizations, for example, grant credits to the country in difficulties, that country would have to follow the organization's recommendations concerning its commercial policy towards non-Community participants of the organization.

If such steps prove inadequate, the Treaty provides other means to prevent trade diversions when the country in difficulties maintains or re-establishes quotas on products from non-Community countries. This implies that the country in question will be able to re-establish quotas on non-Community products but that it will not do so on Community products, particularly if Community countries grant mutual assistance. Only in the absence of mutual assistance, or in case of its inadequacy, could the Commission authorize the country in question to re-establish quotas on Community goods. Even here the implication of the Treaty's spirit is that quotas on Community goods should be less rigorous than those applicable to non-Community goods.

One may well wonder, however, whether these provision can be given effect in their entirety, in view of the obligations of the Community countries towards I.M.F. and G.A.T.T. now that European currencies have become convertible. If it is true that, on the one hand, the rules of the G.A.T.T. relating to customs unions do not contemplate the possibility of preferential treatment within the union in regard to import quotas, and on the other hand, that the import quotas applied by countries subject to balance-of-payments difficulties must be applied in a non-discriminatory way, it is legally impossible for a Member State to impose quotas on non-Community goods and not on goods originating in other Community countries.

53 See text at note 35 and following paragraphs.
54 See pp. 142-44 supra.
From a legal viewpoint it would seem that this will continue to be true so long as the Member States have separate currencies and separate quotas in the eyes of I.M.F.

These are legal conclusions, and it is not absolutely certain that the Six would agree with the interpretations of G.A.T.T. here suggested. It is quite possible, however, that events will obviate the need to consider such problems, for at present both the Six and the other industrial countries of Europe are moving towards as complete and rapid an elimination, on a non-discriminatory basis, of the whole quota system as is possible.

D. The Principles of the Common Commercial Policy

In establishing their customs union, the Six of course had to take into account its repercussions on their commerce with third countries. This preoccupation became more and more central as the months passed, and it is now the major one of the Community and of its European and non-European associates.

A number of Treaty articles define the Community position in regard to the important international commercial problems raised. Article 18 provides: “Member States hereby declare their willingness to contribute to the development of international commerce and the reduction of barriers to trade by entering into reciprocal and mutually advantageous arrangements directed to the reduction of customs duties below the general level which they could claim as a result of the establishment of a customs union between themselves.” Pursuant to this article the Community can negotiate reductions of its common external tariff in exchange for similar reductions by third countries. The G.A.T.T. negotiations in 1960 pursuant to the Dillon proposal will be undertaken in accordance with Article 18.

Similarly, Article 29—the last in the section of the Treaty dealing with the common external tariff—states that in carrying out the tasks entrusted to it, the Commission shall be guided by:

(a) the need for promoting commercial exchanges between the Member States and third countries;
(b) the development of competitive conditions within the Community to the extent to which such development will result in the increase of the competitive capacity of the [sic] enterprises.

Allusion to the competitive capacity of Community enterprises recurs in Article 110, which reads as follows:
By establishing a customs union between themselves the Member States intend to contribute, in conformity with the common interest, to the harmonious development of world trade, the progressive abolition of restrictions on international exchanges and the lowering of customs barriers.

The common commercial policy shall take into account the favourable incidence which the abolition of customs duties as between Member States may have on the increase of the competitive strength of the enterprises in those States.

If the over-all result of the creation of the Community is an increase of the productivity of Community enterprises as a whole, they will in fact need less tariff and quota protection against non-Community competition than they now enjoy or even than that which the establishment of a common external customs tariff based on the arithmetical average of present tariffs will afford.

In addition to these declarations of principle, the Treaty provides procedures for the adoption of a common policy and for establishing relations with third countries. Article 111 provides that the Member States shall coordinate their commercial relations with third countries in such a way as to create, by the end of the transitional period, the conditions necessary for a common foreign commercial policy. The Commission must submit to the Council proposals concerning the procedure to be followed during the transitional period to ensure common action and the unification of commercial policy. The Commission is also to submit to the Council recommendations concerning tariff negotiations with third countries affecting the common tariff. These negotiations are to be conducted by the Commission in consultation with a special committee designated by the Council to assist the Commission. Finally, Article 111 provides that the Member States shall, in consultation with the Commission, take all necessary measures to adjust prevailing tariff agreements with third countries in order that the common external tariff may be put into effect without delay.\(^55\)

Finally, the Treaty makes clear that the Member States must, in respect to all matters of particular interest to the Common Market, act in common in international economic organizations (I.M.F., G.A.T.T., O.E.E.C., Food and Agriculture Organization, the U.N. Economic and Social Council, and international groups concerned

\(^55\) This problem, which relates to rights already vested, is treated in this Part III, Section E in Subsection 5 dealing with the Dillon proposal.
with basic raw materials). During the transitional period, Member States are to consult with each other in order to coordinate their action and, as far as possible, to adopt common positions.

The provisions contained in these articles of the Treaty require no special comment. They make abundantly clear that the objective of the Treaty is, in regard to questions of commercial policy, to make of six states one. The following section of this chapter, dealing with the history from its inception of the relations of the Community with third countries, illustrates how these provisions have worked until now and what problems Community and non-Community countries face under existing circumstances.

**E. The External Commercial Policy of the Community Since Its Creation**

**I. Negotiations with Regard to a European Free Trade Area**

The problem of the relations of the Community with other European countries arose before the Treaty was signed (March 1957). In July 1956, the Council of the O.E.E.C. decided to study the possibilities of creating in Europe a free trade zone associating, on a multilateral basis, the customs union envisaged by the Six and the other countries of the O.E.E.C., who would not belong to the union. An expert report published by the O.E.E.C. in January 1957, concluded that the establishment of such an area was a practical possibility.

In a free trade area, as is true of a customs union, all barriers to trade—notably, customs duties and quotas—are abolished in regard to goods from the countries which compose the area. In contrast to a customs union, the free trade area does not involve the establishment of an external tariff common to the countries of the area. Each member state continues to set its own tariffs on goods originating outside the area.

If the free trade area had been established, the result would have been a vast European area, including the Six, within which goods would have circulated freely. The Six would, at the end of the transitional period, have applied the same tariff to goods originating outside the area as they now will—the tariff of the Community—

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56 Treaty art. 116.
while each of the other countries would have applied its national tariffs.

Why did O.E.E.C. envisage the creation of a free trade area rather than the formation of a customs union among its members, that is, rather than a geographical extension of the union contemplated by the Six at that time? The reasons were both political and economic. The European Economic Community is not merely a customs union, and its aims include political unification of Europe in forms which prevent the association of several European countries for various reasons (for instance, Austria, Sweden, and Switzerland for reasons of neutrality).

Moreover, several European countries are low-tariff countries. Should they become members of the Community, they would be forced to raise their tariffs to the level of the future common external tariff of the Member States. This they are not ready to do. Finally, the United Kingdom for obvious reasons could not relinquish the preferential system of the Commonwealth—which she feared would be necessary in order to join the Community.

The choice of a free trade area as the vehicle for unification was imposed by G.A.T.T. rules. As to tariff questions, G.A.T.T. is based on the principle of the most-favored-nation clauses. This principle prohibits new tariff preferences, with the exception of customs unions (which the Six chose) and areas of free trade. These O.E.E.C. countries which are not part of the Community could not agree to form a customs union and had, therefore, only one choice—the free trade area.

The maintenance within a free trade area of different external tariffs in each country of the area obviously raises an important problem which is nonexistent in a customs union once its common external tariff is effective. Since this common external tariff is the same for all customs union countries, all goods originating outside the union pay the same duties regardless of the country of entry into the union. Consequently, such goods may pass from country to country of the union, either in their original form, or after transformation, without the necessity of establishing their origin, since they will have paid—at whatever point of entry into the union—the duty contemplated by the common external tariff.

In a free trade area this would not be the case. The countries of the area maintain autonomy over external tariffs. Some of these countries would necessarily apply lower tariffs to given goods imported from outside the area than would others. As obstacles to
free trade within the area are abolished, goods coming from outside the area might enter through the country with the lowest tariffs, or with none at all, passing thereafter into the other countries of the area, and arriving therein at a lower cost than they would have paid had they entered directly.

Where this is possible, the creation of a free trade area could entail abnormal upheavals within the commercial structure. To avoid this, a mechanism is necessary which will permit determination of those products which are absolved from paying duties when traded within the area (such products being considered as having originated in the area) and those which continue to pay duties when they pass from one country of the area to another (these products being considered as having originated outside the area).

Within a customs union then, all products will circulate freely at the end of the transitional period, whereas, within the free trade area, customs barriers will be maintained indefinitely between the various countries of the area in order

1) to determine the origin of goods, and

2) to collect duties on those goods which are not considered to have originated within the area.

The situation within the customs union during the transitional period is analogous to that which obtains permanently in a free trade area. The Six have solved these problems by the rules relative to *libre pratique*, but, as has been indicated, the countries of the Community have found it difficult to resist the temptation to verify the origin of goods. It must be emphasized, however, that the problem is transitory in a customs union and permanent in a free trade area.

Initiated as early as July 1956 (before the Treaty was signed), pursued in other forms in the spring of 1957 (after the signing of the Treaty), taken up again in the fall of 1957 (after the ratification of the Treaty by the Parliaments of the Six), the negotiations relating to a European free trade area, including the Six, were finally suspended in December 1958. The fundamental reasons for this failure cannot be examined in detail here. One, among others, was the opposition of France, which had strongly criticized the very concept of a free trade area, viewing with a jaundiced eye the possibility of subjecting her industry not only to the competition of the other five Member States but also to that of other European countries. Moreover, the creation of a free trade area including the

58 See p. 125 supra.
customs union of the Six would have, in the view of some, weakened the Community to the point where it would have lost its special character, thereby compromising the realization of those political objectives which it is also pursuing.

More significantly, however, the European countries were unable to agree on a system of definition and determination of the origin of goods. Moreover, it ultimately became clear that this problem is directly related to the problem of the freedom of the countries of the area to modify, during the existence of the area, their commercial policies vis-à-vis third countries. A system of origin definition designed to avoid diversions of trade, and taking account of tariff levels of the respective countries of the area, might well become ineffective if these countries were to preserve absolute freedom to alter tariff levels vis-à-vis third countries.

Assume, for example, that one country of the zone applies a duty of 20% and another a duty of 30% to imports of a given raw material from countries outside the area. If, according to the rules of the area, products manufactured from this raw material will be considered to have originated in the area if their value is double that of the raw material, the difference in customs costs incorporated in the finished product will be \( \frac{30\% - 20\%}{2} \) or 5%. At the outset this difference may not be thought to falsify competitive conditions, because transportation costs and levels of productivity may compensate, and the difference can therefore be absorbed. If the country which applied a duty of 20% now reduces it to zero, the difference in customs costs becomes \( \frac{30\%}{2} \) or 15%, which represents a substantial difference in the cost of bringing the product to market. This difference could cause diversions of trade and other commercial activity, and the only way to alleviate its effect would be to change the rules concerning the determination of origin—for example, by providing that a finished product cannot be considered to have originated in the area unless its value is five or six times that of the imported raw material which it contains. In order to avoid the necessity of constant modification of the rules for determining origin and to keep countries from abusing their freedom to modify tariffs at a moment’s notice, that freedom must be limited.

All of the European countries were ready to agree that freedom in this area should be limited by controls or sanctions, but they were unable to agree on the scope of the limitations to be imposed. Some
wanted a rule that no member could alter its tariffs on goods from non-members without prior agreement of the other members. Others, rejecting controls of this kind, suggested that it should be possible to change the rules concerning definition of origin if a country were to change tariffs vis-à-vis third countries to an extent which would create trade diversions within the area. In such a case, it would be possible to deny to the relevant goods the customs benefits otherwise granted by members of the area to goods of the others.

The suspension of the free-trade-area negotiations created certain difficulties in Europe, and no one yet knows how they can be resolved. After the negotiations had been broken off, seven countries of Europe which do not belong to the Community (Austria, Denmark, Norway, Portugal, Sweden, Switzerland, United Kingdom) discussed the possibility of creating among themselves a free trade area which would be independent of the Community, and the Community found itself confronted by a new situation which brought it to adopt concrete measures with regard to third countries, and to take up the general problem of its relations to non-Community countries with a particular sense of urgency.

2. SPECIFIC MEASURES TAKEN ON JANUARY 1, 1959, WITH REGARD TO THIRD COUNTRIES

The halting of the free-trade-area negotiations, the European crisis which resulted, the accusations of discrimination brought against the Community, and the fact that it was considered guilty by many of provoking a split of Europe into two groups—all motivated the Community to take certain measures vis-à-vis non-Community countries on January 1, 1959. On that date—it should be recalled—the Six were required, as among themselves, to

1) lower their customs duties by 10% and

2) increase import quotas by 20% on Community goods (having first combined those applying to goods from the other five into single global quotas).

By a decision dated December 3, 1958, the Council ruled that the Member States should, on January 1, 1959, reduce by 10% duties on industrial products with a rate higher than that of the future common external tariff but not to a level below that of the common external tariff. This reduction was effected in regard to O.E.E.C. members, G.A.T.T. members and non-members of G.A.T.T. who have most-favored-nation treaties with Member States of the Com-

An appendix to this chapter examines the European Free Trade Association (E.F.T.A.) organized by these seven countries.
munity. The decision of December 3 provided that, subject to the reciprocal grant of like benefits, Community countries should increase quotas on industrial products from O.E.E.C. countries by an amount equal to 20% of the total value of quotas of each of the Six in favor of other O.E.E.C. countries. Within the framework of this over-all increase, it was required that each quota should be increased at least 10%. The second instalment of 10% was not necessarily to be applied to each quota, but could be used for products of special interest to the country in question and in particular for those products which are subject to insignificant quotas or in regard to which no quotas have been opened.

These measures meant—as far as tariffs were concerned—that:

1) by decreasing duties on imports from non-Community countries by 10% (as they had in regard to Community goods), the Member States avoided discrimination against non-Community countries in implementing the E.E.C. Treaty;

2) by limiting this decrease to duties on those products which were subject to a higher duty than that of the future common external tariff of the Community, they took the first step, as of January 1, 1959, towards the creation of a common external tariff (although the Treaty provides only that the first decrease of external tariffs should take place on December 31, 1961), thereby anticipating by three years—and on their own initiative—the Treaty schedule, although nothing required them to do so; and

3) by restricting the decrease to duties which were higher than the duties of the future common external tariff, the Member States have nevertheless introduced differences of treatment of Community and non-Community countries since they also reduced by 10% duties on Community goods which were inferior to the common external tariff without extending this reduction to third-country goods. It would, of course, have been foolish to extend this reduction to third-country goods since such a reduction would have affected duties which, on December 31, 1961, would have to be raised again in order to progress towards the level of the future common external tariff.

These tariff measures affecting third-country goods, having been thus determined, were duly put into effect on January 1, 1959, at the same time that the tariff reductions on Community goods were effected. In fact, however, their implementation in some sectors has been retarded, because the future external tariff of the Community was not yet known. This forced the Member States to fix approxi-
mate duties, choosing levels which seemed likely to be higher than those of the future common external tariff. A special difference in treatment resulted in certain cases from the fact that as to a few products some of the Member States took as a base the duties applied on December 31, 1958, whereas these duties had been partially or totally suspended on January 1, 1957, the determinative date of basic duties under the Treaty. Since the duties to which the 10% reduction was applied were different, the result was, of course, that lower duties were put into effect on Community goods than on non-Community goods.

Country by country, the situation was this:

1) Germany had of her own accord reduced duties on a great number of imports from the entire world. These reductions, effected after January 1, 1957, were taken into account in applying the provisions of the Treaty, and Germany had to make only a few new tariff reductions on imports from Community, as well as from non-Community, countries. These few were made and, as far as industrial products were concerned, in a generally non-discriminatory manner.

2) Tariffs of the Benelux countries were, in general, lower than the future common tariff of the Six. Benelux reduced its tariffs by 10% within the Community, but, of course, did not effect the same reduction on all third-country goods. Where the then applicable tariff was higher than the future external tariff of the Community, however, the same 10% reduction applicable to Community goods was put into effect.

3) Italy gave effect to the 10% reduction on goods from third countries, but made exceptions of a great number of products in regard to which it was difficult to predict whether the external tariff of the Community would be higher or lower than the applicable Italian tariff.

4) France's procedure was similar to Italy's. She had, in 1957, however, reduced or suspended duties on certain products (paper pulp, kraft paper, boxes) but these reductions and suspensions were later repealed. Under the terms of the Treaty, France was obligated on January 1, 1959, to fix tariffs within the Community 10% lower than those actually applied on January 1, 1957. As to non-Community goods she put into effect tariffs which were 10% lower than those provided for by law on December 31, 1958. This difference can be fairly important. For instance, on raw pulp the legal duty of 22% had been suspended on January 1, 1957, and one of 6% was
in fact applied. On January 1, 1959, the tariff to be applied to Community goods was therefore fixed at 5.4%, while the one applied to third-country goods was fixed at 19.8%.

The decision of the Six of December 3 meant, as to quotas, that these countries offered to other O.E.E.C. members bilateral negotiations concerning the application of the Treaty rules, with the exception of the rule of 3% relating to small or nonexistent quotas. This negotiation in fact fixed the over-all increase of quotas at 20%, whereas the implementation of the 20% rule resulted in an increase of much more than 20% of the quotas among the Six. No unanimous decision of the Council of the O.E.E.C. could be reached concerning this offer to negotiate, and each country was left free to initiate bilateral negotiations with one or another of the Six. Actually, such negotiations took place only between France, and most of the countries now constituting the E.F.T.A. Their result was a substantial increase in the quotas opened by France to these countries subject to the grant of reciprocal benefits by them—an increase which in the French-British case, far surpassed the 20% maximum.

3. THE REPORT OF THE EUROPEAN COMMISSION OF FEBRUARY 1959 ON FUTURE RELATIONS OF THE SIX WITH OTHER EUROPEAN COUNTRIES

Following the suspension of the negotiations concerning the free trade area, the Council gave the Commission the task of preparing a report concerning possible solutions of the problem of relations between the Community and the other European countries. The report of the Commission was submitted in February 1959, and even though it was not approved by the Council, it is highly interesting in that it indicates what preoccupies the Commission.

The report states in particular that the relations of the Community with the other European countries should be viewed within the framework of a general world-wide policy. From this point of view, protectionism would be an inconceivable Community policy. It is incumbent on the Community to pursue a liberal policy in regard to Europe and the rest of the world and to translate its intentions into actions. Noting that the United States, the United Kingdom, and the Community carry on almost one half of world trade, the Commission stated that these great industrialized economic entities have a particular responsibility in maintaining the economic equilibrium of the world. The major part of the world is, it continued,
composed of countries which are still in the throes of development, and it is doubtful whether they can, on their own, develop their national economies satisfactorily. Therefore, freer trade in the world will only be possible if it goes hand in hand with active and coordinated development programs. Experience demonstrates that free trade alone is not equal to the task of eliminating too-great disparities. On the contrary, if other steps are not taken, free trade may result in widening the gaps between rich and poor countries. The Commission therefore proposed a common policy to be followed by the United States, the United Kingdom, and the Community, with a view to lowering tariffs on a world-wide scale, to furnishing technical and financial assistance to developing countries, primarily by means of export credits, to stabilizing the prices of raw materials, and to assuring world-wide coordination of policies designed to meet problems created by business cycles.

Having placed the problem of the relations of the Community with the other countries of the O.E.E.C. in the more general framework of relations with the world as a whole, the Commission nevertheless reaffirmed the absolute political necessity of European solidarity. Although it rejected the concept of the free trade area as a means of associating the Community with other European countries, it nevertheless proposed some concrete tariff measures in order to establish a modus vivendi among O.E.E.C. countries.

Primarily because the propositions of the Commission were inadequate at the European level, the Council could not approve the Commission's report. In March 1959 it therefore appointed a special committee to formulate suggestions for reviving negotiations with other O.E.E.C. countries directed at the creation of a multilateral association between them and the Community. This special Committee has not as yet completed its work, and in the meantime, seven countries of the O.E.E.C. have decided to create among themselves a free trade area.60

4. THE PROBLEM OF THE HARMONIZATION OF COMMERCIAL POLICIES IN REGARD TO CERTAIN COUNTRIES

Even though the Community has often reaffirmed its intention of pursuing liberal commercial policies in regard to non-Community countries, the lack of a common commercial policy during the transitional period will create certain problems. Because one of the Six

60 See appendix at end of this chapter.
applies a more liberal tariff or quota to a given non-Community product than another, a risk of trade diversions within the Community, which will provoke lively reactions on the part of the producers, will result. The highly-developed countries which make up the Community are particularly afraid of the competition of three groups of countries:

1) those which have abnormally low salaries and wages (that is, the developing countries in Southeast Asia);
2) those where the state enjoys a commercial monopoly (the countries behind the Iron Curtain);
3) those which use artificial methods of a kind which falsify the price of exported products (for instance, countries with multiple exchange rates).

The risks of trade diversion during the transitional period are connected to the problem of fibre pratique within the Community, and, in the cases of trade diversion, the countries may invoke the safeguard clauses of Article 115.61

Confronted with these problems, the institutions of the Community have assigned the Economic and Social Committee (a consultative organ which represents economic and professional interests) the task of dealing with them. In July of 1959, this Committee submitted to the Commission an opinion representing the viewpoint of economic and professional groups on these problems. This opinion indicates that, if the agreement of the Six on a common commercial policy (which, according to the Treaty, is the ultimate goal for the distant future) cannot be reached immediately, lack of coordinated action in regard to the three groups of countries mentioned above may well cause free trade in certain products 62 within the Community to fail. The reason for this is the possibility of recourse to the measures contemplated by Article 115 of the Treaty. The coordination of commercial policies of the Member States, which the Treaty foresees for the transitional period, should, in general, be effected without delay, according to this opinion, and ought to be begun immediately in cases where the above-mentioned danger threatens.

In this connection, the Economic and Social Committee has formulated a certain number of proposals which, it seems, have not as yet been seriously examined by the Community institutions.

61 See text at note 32 supra.
62 The products in question are both industrial and agricultural, for example, natural or artificial textiles, optical goods, certain metal products, sewing machines, ceramics, rubber footwear and toys.
It is interesting to note that the spirit of these recommendations is to some extent protectionist in regard to the exports of the countries in question. Increased protection against exports of certain countries—and notably of those whose economies are in the throes of development—plainly seems to contradict the liberal declarations of principle of the Commission and to negate its professed desire to contribute to the development of these countries. No hasty conclusions should be drawn, however, since these are special cases which do, in fact, create problems of a certain gravity for the European industries affected.

5. THE DILLON PROPOSAL FOR REDUCTION OF THE TARIFFS OF THE PARTIES TO G.A.T.T.

At the session of G.A.T.T. held late in 1958, Mr. Dillon, as head of the United States delegation, submitted a proposal looking to a new multilateral tariff conference (analogous to those held at Annecy, Torquay, and Geneva during the last ten years) which would permit the President of the United States to utilize the powers, granted him by the Reciprocal Trade Agreement Extension Act of 1958, to reduce existing U.S. duties 20% on all products (with the exception of those duties which have reached the "peril point"). These powers expire on June 30, 1962.

In accordance with this proposition, G.A.T.T., during the winter of 1958–59, studied the possibility of organizing such a conference. The interest of this proposition obviously lay in bringing about a lowering of U.S. duties, as well as those of European countries, and particularly, those of the Common Market, thereby making new progress in the direction of liberalized world trade.

Realization of the Dillon proposal will create problems, however, from the point of view of the Community. The first of these is whether the Member States should negotiate on the basis of their present tariffs or on the basis of the future common external tariff. The answer is, as it were, imposed by the future common external tariff. In view of the fact that during the years to come the Treaty requires Member States to raise their duties on some of their products, and to lower them on others in order to establish their future common external tariff, it would be illusory to obtain concessions from them with regard to duties which they will, in any case, have to lower or with regard to others which they must in any case increase later.

A second question results from one of the rules of G.A.T.T. The
countries of the Community will have to increase certain duties to place them at the level of the common external tariff. A large number of these duties have been "bound" by each Member State vis-à-vis third countries. These commitments resulted from prior tariff negotiations—a given Member State agreeing, in exchange for counter-concessions by other G.A.T.T. countries, to reduce and "bind" certain of its duties, that is, not to increase them. It is clear that if one of the Member States is to increase a "bound" duty in order to carry out its obligations within the Community, then it must either give up such counter-concessions or offer other compensation. This compensation may, of course, result from the fact that another Member State must lower corresponding duties to place them at the level of the future common external tariff, and G.A.T.T. expressly provides that situations of this kind should be taken into account.

The effect of these provisions is that the ultimate establishment of the future common external tariff of the Community requires not only that the Member States shall fix this tariff in accordance with the complex rules already described, but that the "bound" tariff headings which the Member States intend to increase to the level of the future common external tariff should be re-negotiated with the countries of G.A.T.T. which are not members of the Community. This tariff will, in effect, be modified following these renegotiations because the Member States of the Community will have to offer compensation to their G.A.T.T. partners.

Consequently, if negotiations are undertaken pursuant to the Dillon proposal on the basis of the future common external tariff, it will be necessary to carry out successively two separate negotiations—one to re-negotiate the "bound" tariff headings of the Community members, and the other, on the basis of the external tariff of the Community resulting from such re-negotiations, to lower the common external tariff in exchange for counter-concessions by the United States and other countries.

By a decision of May 5, 1959, the Council decided to accept the offer of Mr. Dillon so that new tariff decreases can be effected in the interest of developing world trade. The Council considered that this objective is perfectly in accord with the intentions of the Member States as expressed in the Treaty, according to which the Common Market should contribute, in conformity with the public interest, to the harmonious development of world commerce, and, especially, to the reduction of customs barriers.
At its 1959 spring session, G.A.T.T. was able, therefore, to decide to hold a new world tariff conference. This is to begin on September 1, 1960, at which time the "bound" duties which the Member States of the Community intend to raise will be re-negotiated. The conference should end by Christmas 1960. In January 1961, the negotiations of the Dillon proposal itself will begin. They are to be terminated in time to make it possible for the President of the United States to use his powers to lower U.S. tariffs.

This schedule plainly has meant that the Member States have had to accelerate their decisions regarding the projected common external tariff. This tariff had to be ascertained as soon as possible in order that the countries of G.A.T.T. could know which tariff headings were to be re-negotiated, and what concessions would be asked of the Member States, either by virtue of an "unbinding" of these headings or in order to obtain from the Six reductions of their future common external tariff (within the framework of the Dillon proposal) in exchange for appropriate counter-concessions.

IV. CONCLUSIONS

A. DIFFICULTY OF FORMING JUDGMENTS

An examination of those provisions of the Treaty which relate to the elimination of obstacles to trade among the Member States and to the establishment of a common external tariff and commercial policy indicates that, although the Six were successful in establishing fairly precise rules concerning their relations with each other, they were forced to leave vague the greater part of the rules affecting relations with third countries. This is understandable—among themselves the Six could undertake firm mutual obligations, because each was in a position to evaluate the benefits to be received in exchange for benefits granted, and to give effect to the benefits it promised. On the other hand, the establishing of a common external policy raises complex problems in view of the very different initial positions of the Member States, some traditionally liberal and others traditionally protectionist. Moreover, this is a field in which the countries in question have only partial control since they are bound by other international obligations and since foreign policy may only be defined in relation to constantly evolving situations at home and abroad.

It is practically impossible to take stock now of the effect of the internal rules of the Common Market. The goal is clearly enough
defined—the establishment of a single economic unit grouping highly industrialized countries whose population, economic power, and technical capacities will make it the third-ranking economic power in the world. But how will this be accomplished? Will the rules of the Treaty governing the abolition of tariffs and quotas be strictly applied? What scope will be given the safeguard clauses invoked? In particular, will the clause relating to difficulties pertaining to a particular sector be applied sparingly or will it be used to shield large areas of economic life from the full force of the Treaty? Doesn’t the flexibility of the system for the abolition of tariffs involve the risk of postponing the solution of the thorniest problems until the end of the transitional period and, won’t the consequence be virtually insoluble difficulties? It must be remembered that some Member States have long protected their industries extensively, and exposure now to competition with those of other Member States will create real problems.

It is also clearly difficult to estimate the effects of the rules governing the elimination of obstacles to trade among the Member States without taking other rules into account. For example, the rules concerning state competition and competition among enterprises must be considered. All state subsidies to industries are to be abolished, but how is this principle to function and what will be its consequences? Again, cartels and all forms of understanding between private enterprises are, as a matter of principle, prohibited. But, in spite of this prohibition, isn’t there a risk that enterprises of the various countries may come to understandings dividing markets among themselves in order to avoid competition which is too lively for their tastes? What will be the impact of the ultimate answers to these questions on the structure of enterprise—will the smallest disappear, victims of powerful combinations, or will small enterprises be able to survive? What effects will this have on commerce? What kinds of professional groups will be established?

Another and a related question—what will be the balance of power between producers and consumers within the Common Market? For the time being, it seems that producers have more rapidly recognized the importance of what lies ahead and that they are organizing effectively at the Community level. No similar organization seems to exist among consumers. The unions are divided by politics, and not yet ready to take advantage of the new situation to increase international trade-union cooperation. However, things may change—though how and when no one can tell.
Even though the Treaty envisages some harmonization of the fiscal policies of the Member States, it imposes no firm obligations. It is therefore difficult to imagine what will happen in this area, since these policies will obviously exert great influence on any changes in the structure of enterprises, on their possibilities of investment, and on their respective competitive capabilities in the various countries of the Community.

Under these conditions, although in theory it is possible to assert that the creation of the European Economic Community will strengthen the economic power of its Member States by increasing the competitive capability of the whole and by raising the standard of living of Community inhabitants, it is difficult to determine to what extent and at what pace this will be accomplished, and also what sacrifices will be necessary and what economic upheavals will precede it. Will productivity rise faster or will wages—or will the two be subject to a "see-sawing" effect? And to what extent will balance-of-payments crises obstruct the course of events?

In this respect, it is obvious that the key to success in establishing the Community is the maintenance of a high level of economic activity. Only within the framework of a continuous increase of production, productivity, and total consumption will the countries of the Community be able to accept the necessary economic and social changes. If marginal enterprises have to shut down, it is essential that, through the continual progress of the economy as a whole, the workers thus freed may immediately find other employment. The Common Market could not survive a major unemployment crisis. The resulting political and social reactions would immediately force the governments to take protective measures, particularly with regard to imports, which would negate the very principles of the Community and would lead to its failure. But it is impossible for the Six to study economic trends in isolation—they must consider those in the rest of the world, and particularly those in the United States and the sterling zone. The internal success of the Community therefore depends directly upon policies adopted beyond its boundaries.

This raises the problem of the external policy of the Community itself. The provisions of the Treaty in this respect are vague. Moreover, the future common external tariff of the Community will give rise to negotiations the over-all results of which cannot be foreseen—all the more reason why it is impossible to predict what tariff will be applied to any particular product.

How will the external policy of the Community be determined?
In the first place, the degree of success of the Community's internal policy will be a factor. If, in the abolition of the obstacles to the free flow of goods among themselves, the Member States encounter great difficulty, a protectionist attitude towards the rest of the world will automatically result. If they succeed in eliminating commercial obstacles smoothly, however, there is every chance that their attitude towards the rest of the world will be more liberal. The Treaty itself provides that, in establishing its external commercial policy, the Community shall keep in mind the increase of competitive capacity which would normally be expected to result from the establishment of the Common Market.

The common external policy of the Community will also be influenced by its obligations towards its own overseas and associated territories. In so far as it wants to give the latter preferential treatment, it will have to maintain barriers against third countries.

The policy will also depend on the policies of other countries, both commercial and other. In this respect, initiatives such as the Dillon proposal and the creation of the free trade area of the Outer Seven will undoubtedly have an effect.

Finally, other international obligations of Community members will also play an important part. The provisions of the Treaty relating to the abolition of quotas among the Six, as well as the problem of a common quota policy, appear today in an entirely different light than they did at the time the Treaty was negotiated. There is no excessive optimism in the statement that, within a relatively short period, European countries in general, and those of the Community in particular, will most likely give up the system of quotas as a systematic means of protection against imports. This movement will be to the advantage of third countries, especially the United States. It will also result in a more liberal orientation of the Community than could have been expected only a short time ago. Another consequence, however, will be an increase in the importance of tariffs which will remain the only means of protection for Community products.

However, the freeing of imports and the durability of measures of liberalization are in direct correlation with stability in balances of payments and dependent upon financial, monetary, and economic policies adopted both by the Member States and by the larger non-member countries. In case of recession, general recourse by Community states to quotas will seem normal and is virtually certain. Here again, a coordination of economic policies of Europe and the
United States is imperative to avoid serious troubles and a retreat from the liberalization of world commerce.

The countries of the Community are all large importers of basic raw materials, and these imports should normally increase as the economic strength of the Community increases. The role of the Six in the commerce and economic development of the underdeveloped countries will therefore be an essential one. The Community is well aware of this role, but to play it adequately, the Community must pursue liberal import policies vis-à-vis these countries—a necessity which creates conflicts. For some Member States want to maintain or even increase their production of some raw materials, but many such enterprises could not survive third-country competition. The Community also wishes to maintain preferences in regard to the African territories with which it is associated. How these conflicts will be resolved no one can guess.

To sum up, and granting the uncertainties remaining in regard both to the internal development of the Community and to its relations with the rest of the world—and in spite of the setbacks which it may suffer in the course of its evolution—one cannot doubt that the formation of a new economic group as powerful as is the Community marks a major event in the history of the economic and commercial relations of the world.

Its formation will in all likelihood substantially strengthen the competitive capacity of the enterprises of the Community. In addition, the products of each Member State will benefit from tariff concessions of the others, for—in contrast to non-Community goods—they will ultimately be free from import duties. Consequently, the competition of Common Market producers will be more and more active both in Community markets and those of third countries. This competition, however, should provoke a lively competitive reaction in third countries, and it is to be hoped that in the end the main beneficiaries will be consumers in the Western world as a whole. The spectacular rise in the standard of living in Europe that occurred after the Marshall Plan was inaugurated ought logically to continue, and it will entail a substantial increase in the needs of European countries for basic raw materials as well as for machinery and consumer goods. All in all, although the nature of trade currents may change, it is unlikely that their volume will decrease.

These are the general conclusions usually drawn with respect to

63 See the “Hallstein Report,” discussed in Part III, Section E, Subsection 3.
64 See the discussion concerning List G in Part III, Section A, Subsection 4.
the creation of the Community and, subject to the maintenance of boom conditions in the world, there is reason to believe that these conclusions will be verified by experience.

The existence of this new group will certainly involve some general problems for the United States concerning both the world's political and its economic balance. It is difficult to say how the overall balance of payments of the United States will be affected. Some American industries will encounter greater competition in Community markets as well as in third-country markets and even in those of the United States. The demand for the products of other industries will increase. On the other hand, if the countries of the Community participate increasingly in financing investment in underdeveloped countries, the United States' share of the burden will, perhaps, be relatively lightened.

The conduct of the United States will greatly influence the policies of the Community. A shift towards protectionism would produce a similar shift in the Community, and a resolutely liberal U.S. policy will encourage liberal tendencies in the Community. Moreover, coordination of policies to control economic cycles will be an essential element of the effort to free trade throughout the world. Increased American investment in the Community alone will not compensate for the potential harm to U.S. industries which the creation of the Community could cause. Above all the United States must seek bases for active cooperation with the European countries directed at the maintenance of world prosperity, assistance to underdeveloped countries, and total freedom of trade. In this audit of the uncertainties which weigh so heavily on the future of the Community these conclusions alone are certain.

B. LESSONS DRAWN FROM THE EXPERIENCE OF THE FIRST MONTHS OF THE COMMUNITY

Can one draw conclusions from the history of the first months of the Community? Probably not, but it is certainly useful to isolate outstanding factors, since they will dominate its evolution in the months or years to come.

The first tariff reductions and quota increases within the Community were, generally speaking, carried out according to the rules of the Treaty. They seem to have raised no difficult problems for the Member States, nor of themselves to have had serious consequences for other countries.

These reductions and increases were, of course, fairly modest
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in terms of absolute values. A 10% reduction of tariffs reflects a minimum effort at best. The increase of quotas was more impressive—in fact, larger than the Treaty provided for, but it occurred in circumstances which necessarily made its effect negligible. On the other hand, these advantages have also been granted in a relatively non-discriminatory manner to third countries.

The conditions under which this was done in regard to tariffs have already been indicated. The efforts to be made by the Benelux countries, Germany, and Italy in regard to quotas were of only minor importance, but, particularly as a consequence of the convertibility of currencies (and in the case of Germany, under pressure of G.A.T.T.), these countries have in general liberalized quotas on third-country goods to the same extent as quotas on imports from O.E.E.C. members.

France, who in 1958 applied a strict system of quotas on all imports, achieved 94% liberalization within the O.E.E.C. within a few months, and 70% vis-à-vis the dollar area. As to products not yet liberated, she increased quotas within the Community in accordance with the Treaty. She also increased quotas on imports from various other European countries in keeping with bilateral agreements. Because of the devaluation of the French franc and the very strict policy of financial orthodoxy since pursued, as well as by reason of the renewal of confidence created by the government of General de Gaulle, the rapid and extensive removal of restrictions on imports was not followed by a disturbing increase of purchasing abroad.

In sum, then, the Treaty and the measures taken with regard to third countries had no noticeable effect on the volume of imports or on the direction or nature of the flow of trade either within or without the Community.

Indications of a tendency towards protectionism within the Community on the one hand, and a psychological climate favorable to some deflection of the normal flow of trade on the other have already been noted. Protectionism manifested itself in the difficulties which arose in the calculation of the increase of quotas among the Six in accordance with the rules of the Treaty, and especially in regard to the so-called 3% rule. In other areas (particularly agriculture) some states have manifested a tendency to replace tariff or quota protection by consumer taxes on imported products. This development has had the incidental effect of drawing attention to the need of a more immediate and thorough supervision by the Community of
the fiscal policies of its Members than was contemplated at the time the Treaty was negotiated.

Changes in the flow of trade have been accompanied by two groups of contradictory phenomena. On the one hand, cartel agreements have been concluded between or among competing enterprises within a particular country, as well as within the Community. Apparently these agreements are of a financial and technical nature and it is often suggested—although to prove it is impossible—that these firms are organizing to "rationalize" competition among them. Whether these arrangements conceal clauses enjoining excessive competition or providing for a division of markets is also impossible to state.

On the other hand, preparations for an increased exchange of products among the Six are going forward. Business firms of the Six are setting up commercial networks of agents, distributors, and concessionaires in the Community, which, if not yet active, are making preparations for future conquests of markets. The newspapers in each of the Community countries are filled with publicity concerning products manufactured elsewhere in the Community. All of this is new because exporting firms were never sure in the past whether they were going to get import permits from neighboring countries or not. Now they have an almost absolute guarantee that the import policy of the other countries of the Six will become more and more liberal as time goes on. Consequently, they are prospecting markets and organizing outlets to an extent which they would never have considered a short while ago. Finally, because of the preferential tariff system which will progressively take effect, Community agents, representatives, concessionaires, and old clients of non-Community exporters seem tempted to abandon established contacts in favor of new ones with Community exporters. This tendency is obviously not easy to check on, but it is recurrently alluded to.

When the Treaty went into effect, a psychological shock to the public opinion of the Member States doubtless occurred. Public interest is indicated by the abundance of literature on the Common Market and also in the rapprochement of the Six, not only in industrial and commercial areas but also in areas where it would have been difficult, a priori, to imagine that there would be a need for professional organization. It is certainly normal for producers of chemical products, of industrial equipment, and the like, or for
wholesale and retail merchants of the Six to form professional organizations to deal with their problems. It is somewhat astonishing, however, that doctors, pharmacists, and lawyers of the Six are also forming professional groups.

Facts of this kind are evidence of the existence and personality of the Community. There is, indeed, a decided tendency within the Community to assert the existence of this personality by protectionist measures. Without going so far as to defend autarky as an ideal, the partisans of the Community, during its first months, defended relatively high tariffs, as well as the maintenance of quotas on non-Community goods on the basis of a need to set the Community off from the rest of the world. The political objectives of the Community obviously serve to support such theories, which were expressed (especially in France) most forcefully at the time when negotiations were in progress to unite Community and European non-Community countries in a free trade area of the seventeen O.E.E.C. countries. One of the arguments against this area was that it would absorb the Community in larger entity and would ultimately obliterate its distinctive characteristics.

It is all the more interesting to note that, in reaction against this theory, the Member States have in fact extended to third countries a very substantial part of the benefits of the tariff reductions which they made available to each other on January 1, 1959, and that all the members, and notably France, have made a great effort to apply liberalized quotas on a far broader geographical basis than that of the Community. According to the statements of its leaders, the Community also intends to commit itself resolutely to a liberal commercial policy.

These declarations of the intentions of the Community are explained by several important factors:

1) The suspension of negotiations concerning the free trade area among the seventeen countries of the O.E.E.C. caused a crisis in Europe—the gravity of which is clear to all—and the Six wish to resolve it. A few of them, and particularly Germany and the Benelux countries, have very potent economic reasons for wanting to maintain and develop close cooperation with the other countries of the O.E.E.C. by lowering commercial barriers.

2) The convertibility of European currencies established in December 1958, as well as the considerable increase of dollar reserves in the countries of the Community, did away with the justification
for a quota system on imports, whatever their origin, and the Six
are bound by their other international obligations to make further
efforts to liberalize trade.

3) The increase of the competitive capacity of European business and its success in the export trade, especially in U.S. markets,
have eased the fears of European producers concerning foreign
competition, and have led them to look forward more optimistically
to a world-wide liberation of trade.

4) The reversal of the balance of payments of the United States
has weakened the conviction that Europe will eternally be a debtor
of the dollar area, and has also reminded the countries of Europe
of their obligations to the United States, which has contributed so
much to their prosperity, notably by means of the Marshall Plan.
This reversal should be considered in connection with the necessity,
ever more evident, that Europe share with the United States the
burden of aiding the under-developed countries by adopting, vis-à-vis
these countries, liberal commercial policies.

A progressively developing tendency towards commercial liberalism is evident in Europe, then, and particularly among Community
countries. At the same time specific demands for protection in vari-
ous areas have been voiced. Nevertheless the tendency to liberalism
persists, and may well be intensified by rivalry between the Com-
munity and the free trade area of the Seven. Developments in these
two groups will be extremely interesting to watch—particularly the
measures which they adopt in regard to tariffs on July 1, 1960.
Finally, the tariff concessions which European countries are pre-
pared to consider within the framework of negotiations on the
Dillon proposal will be a very important element for the future of
European neo-liberalism.

C. THE UNITED STATES AND THE COMMON MARKET

The effects of the Common Market on the United States have
already been the subject of a great deal of discussion. Commercial
consequences as well as the consequences for the U.S. balance of
payments have been considered. The general opinion seems to be
that the United States accepted the Common Market for political
reasons, and that its effects will be harmful in the short run for
American exports to Europe and elsewhere. In the long run, how-
ever, it will slowly become advantageous as consumption in Europe
increases. To avoid the possible harmful effects of the Common
Market and to profit from the expected burgeoning of economic
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power and prosperity of the Six, many American firms are developing investments in the Common Market.

These views of the probable effect on the United States are perhaps realistic, but, for the reasons already indicated, a prediction that they will prove to be well-founded is difficult to make. It is even more difficult to indicate whether in any particular sector of the economy, or in regard to any type of product, American exporters and producers will show a profit or loss, whether long, short, or medium term. Such a prediction would necessitate a structural study of each sector as well as knowledge of the future fiscal, tariff, and investment policies of the Member States.

If it is assumed that conditions will remain static, one can in fact guess that some trade which presently flows in long-existing commercial channels will be deflected, since consumers of one Community country will find it advantageous to buy in other Community countries, given the fact that imports therefrom will eventually be duty free, whereas imports from third countries will be subject to the common external tariff. Moreover, one may suppose that the competitive capacity of Community enterprises will increase, that marginal enterprises will disappear, and that the concentration of enterprises and mass-production possibilities for a wide market will make Community firms increasingly dangerous competitors for American producers. Indeed, this is the declared aim of the Community. Finally, however, it might also be predicted that, as the European standard of living approaches that of the United States, an increased demand will cause a new surge forward of international commerce, from which American business may also benefit.

What is more important, however, is to know whether and how the United States can influence the commercial policy of the Community, working in cooperation with it and with the other European countries, in order to permit the Community to evolve without setbacks and to create a favorable climate in the Western world for the development and maintenance of prosperity within a liberal trade structure. Action of the United States will be decisive in two spheres: in selecting policies to control the ebb and flow of economic trends; and in freeing the movement of goods.

In this respect the Dillon Proposal for international tariff negotiations was a first step in the right direction. The maintenance of a liberal import policy by the United States is a vital political and psychological element in stimulating the development of liberal tendencies within the Community and in the other European countries.
However, it will be necessary to go further and adopt plans to increase financial and monetary cooperation among the countries of the free world, in order to avoid economic crises which would cause an immediate return to protectionism. The forms of such cooperation are subject to discussion, but the need of it is beyond dispute.

Increased competition between the enterprises of the Community and those of the United States will, then, clearly call for serious efforts by Americans if they intend to maintain and develop markets.

However, these are the "rules of the game" of private enterprise to which the United States is firmly committed. It depends very much on the United States whether the creation of the Community—which aroused serious misgivings among non-Community nations because they sensed, and with some reason, protectionist sentiment within it—will mark a trend towards the lasting creation of a liberal system of world trade and payments.

APPENDIX

THE EUROPEAN FREE TRADE ASSOCIATION (E.F.T.A.) *

(THE LITTLE AREA OF THE "SEVEN")

As suggested earlier in this chapter, the possible association of the six members of the Common Market and the eleven other members of the O.E.E.C. in a free trade area was under discussion within the O.E.E.C. as early as July of 1956. Negotiations towards that end were suspended in December 1958.

In the spring of 1959 seven of the eleven members of the O.E.E.C. who are not members of the European Economic Community (Austria, Denmark, Norway, Portugal, Sweden, Switzerland, and Great Britain) began study of the possibility of forming a free trade area among themselves. During a meeting of Ministers convened in Stockholm on July 20 and 21, 1959, the seven governments decided that the objective of their free trade area negotiations should be a treaty which could be signed and ratified by their respective parliaments in time to permit the area to begin functioning on January 1, 1960. On November 20, 1959, the Convention establishing a European Free Trade Association was initialed by the Ministers in Stockholm and it came into force in spring 1960 upon completion of the ratification process.

* The text of the Convention establishing the European Free Trade Association appears at the end of Volume II of this book.
Now that this project has been realized, the countries of the O.E.E.C. are divided into three groups:

1) those of the Common Market: Belgium, the Netherlands, Luxembourg, Germany, France, Italy;

2) those of the "little free trade area" (the E.F.T.A.); and

3) the still-developing countries—Greece, Ireland, Iceland, and Turkey to which Spain was added at the end of July, 1959, when it became a member of the O.E.E.C.

In creating the Association, the Seven declared that their aim was to facilitate future negotiations with the European Economic Community as well as with other members of the O.E.E.C. (that is, with the still-developing countries) which have particular problems. The object of these negotiations would be the elimination of customs barriers among all members of the O.E.E.C., and the establishment of a multilateral association including all of them, which would make it possible for O.E.E.C. members to increase their economic cooperation and at the same time to further the expansion of world commerce.

The free trade area created corresponds to the general principles of the G.A.T.T. definition of such an area. It contemplates the elimination of the obstacles to trade among its members, who, nevertheless, retain their freedom in regard to questions of commercial and customs policies towards third countries. In order to obviate deflections of trade—which might result from disparities in the commercial and tariff policies of the various participants towards the rest of the world—a definition of origin has been introduced. By virtue of this definition only those products, on passing from one country of the Area into another, which are considered to have originated in the former country will benefit from customs reductions or immunity.

To facilitate the negotiations which may bring together the E.F.T.A. and the Common Market, the seven countries have agreed to rules eliminating obstacles to trade among themselves which are as nearly similar as possible to the corresponding rules of the Common Market. Given the fact that no attempt is made to create institutions of the kind involved in the European Economic Community, the Seven wanted the application of these rules to be as nearly automatic as possible. They therefore made no provision for successive stages in the transitional period during which customs tariffs are to be progressively abolished, thereby rendering unnecessary decisions of the Council of Ministers of the E.F.T.A. concerning the termination of each stage.
The following paragraphs will outline the rules of the E.F.T.A. concerning:

1) the abolition of tariffs,
2) the abolition of quantitative restrictions on imports,
3) the definition of origin, and
4) the safeguard clauses.

The rules relate only to industrial products. Special arrangements govern agricultural products and fisheries.

A. ABOLITION OF TARIFFS

A "basic duty" is fixed. It is the duty which was in force on January 1, 1960. In contrast, therefore, to what was done in the E.E.C., the date determining this duty was not made retroactive. Thus a delay was provided for between the elaboration of the E.F.T.A. Convention and January 1, 1960, in the course of which the members could, as far as their other international obligations permitted, raise their customs duties or re-instate those which had been temporarily suspended wholly or in part. The Seven considered the question, however, whether the basic duty is to be the legal duty or the duty actually applied (that is, one taking into account still existing temporary suspensions). They have adopted a solution which consists in principle in retaining the duty in fact applied, conceding, however, that for certain products individual countries might have legitimate motives for departing from the general rule. A procedure before the Council of the Association is to ensure collective examination of such derogations.

The Seven contemplate a progressive abolition of customs as among themselves, which will take place in the following manner:

1) a 20 percent reduction will be effected on July 1, 1960. In this connection it may be noted that the Six reduced tariffs among themselves by 10 percent on January 1, 1959, and that the second over-all reduction of 10 percent (with a minimum of 5 percent on any single customs duty) is to be effected on July 1, 1960. In lowering their tariffs by 20 percent on July 1, 1960, the Seven hope to catch up with the Six and to fix the tariff reductions which they will at the same time effect among themselves, at the same level as those of the Six (although the plan of the Seven does not manifest the same flexibility as that of the Six).¹

2) Later reductions will follow successively—10 percent reduc-

¹ For the decision by the E.E.C. Council of Ministers to accelerate tariff reduction see Chapter I supra.

This schedule and method mean that the rate of tariff elimination is automatic, allowing no possibility of extension of the transitional period or any part thereof. It means, that the transitional period is much shorter for the Seven than for the Six. It means, finally, that the process is also both automatic and rigid: all customs duties must be reduced at the given dates by the same amount of 10 percent. The Seven have not provided a flexible system of the sort established by the Six. The advantage of the method of the Seven is that it is simpler, avoiding the complex calculations of total customs revenue, and from the outset both governments and businessmen know what to expect. It also avoids the risk of pressure being brought to bear on the governments by special interests. The disadvantage is that recourse to the safeguard clauses in case of particular difficulties of individual industries may be more frequent.

As does the E.E.C. Treaty, the E.F.T.A. Convention provides that each member declares its willingness to lower its customs duties as against the other members more rapidly than required by the rules, if its economic and financial situation and that of the sector concerned so permit. It also provides that the Council may at any time decide that any import duties shall be reduced more rapidly or eliminated earlier and that between July 1, 1960, and December 31, 1961, the Council will examine whether it is possible so to decide in respect of duties applied on some or all goods by some or all of the members.

The Seven have also provided for the progressive abolition of drawbacks, that is, of rebates of duties levied by one member country on goods imported from outside the Area which are subsequently re-exported to another member of the Area after transformation or manufacture. This abolition should be completed by the end of the transitional period.

B. ABOLITION OF QUANTITATIVE RESTRICTIONS

The Seven have, like the Six, provided for a standstill in regard to import quotas. The members may not take steps which would mark a retreat from the level of liberalization reached as of January 1, 1960. Secondly, they contemplate, as do the Six, the complete abolition of all quantitative restrictions on imports within the Area at the latest by the end of the transitional period. To this end they
have agreed to suppress gradually during this period all quotas as between themselves. They hope thereby to avoid neutralizing the advantages obtained by the successive reductions of tariffs on imports and to avoid having to deal with difficult problems at the end of the transitional period concerning quotas which might still be in effect.

To attain these objectives, the Convention contains the following rules:

1) Any quota opened by one of the Seven to another member of the Association must be increased by at least 20 percent per annum;

2) Quotas opened not only in favor of other members but also in favor of third countries must be increased each year by an amount equal to at least 20 percent of the trade actually carried on, within the framework of these quotas, with the other members of the Association;

3) If, for a particular category of goods, a member has provided no quota, or a quota so small that an annual increase of 20 percent would not suffice to achieve complete elimination of the quota by the end of the transitional period, then that member must establish adequate quotas by July 1, 1960. This rule corresponds to the so-called "3 percent rule" for small or non-existent quotas of the E.E.C. Treaty.

4) The increasing of quotas will begin on July 1, 1960, and it will be applied to the quotas in force on December 31, 1959.

In addition, the Seven foresaw two particular quota problems. They recognized that in exceptional cases serious difficulties resulting from the obligation to increase quotas are conceivable within the Area. They are concerned particularly with the case of developing industries, for which a substantial degree of continuing protection may be justified, and with cases where a country applies a very low tariff or none at all, depending solely on quotas as a means of protection. In these cases, the Seven foresaw special arrangements to be authorized by the Council which would permit the complete abolition of quotas by the end of the transitional period and which would not hinder the progressive lowering of tariffs from generating a reasonable rate of trade expansion and which would not create difficult problems towards the end of the transitional period.

The second problem is that of the application of other international obligations, in particular those of the G.A.T.T. and the International Monetary Fund (I.M.F.). The Seven have paid more attention to these obligations than have the Six. Of course, their
The Convention was negotiated at a time when the problem of a world-wide elimination of quotas was being seriously discussed in quite concrete terms whereas when the E.E.C. Treaty was negotiated, the prospects for a world-wide liberalization of trade (made possible in December 1958 when the European currencies became convertible) were still remote.

The Seven declare that they have international obligations concerning the use of quantitative restrictions and that, in establishing the free trade area, they have no intention of modifying those obligations. In particular, they do not propose to use quantitative restrictions in any way to create a preferential regime among themselves. This apparently is the reason for the provision in the Convention according to which quotas opened both to countries of the Area and to third countries will be increased by 20 percent; in fact, although the 20 percent increase is calculated only by reference to that part of the quota used by the other countries of the Area, the quota as calculated will apparently be open to goods from third countries as well as from other members. Moreover, the Seven envisage that during the next ten years the majority of the members of the G.A.T.T. may proceed, in accordance with their international obligations, to abolish quantitative restrictions on a large part of their imports. Accordingly the Council will, by December 31, 1961, and periodically thereafter, examine whether the rules concerning the progressive elimination of quotas continue to be appropriate, and whether, taking account of events occurring after the effective date of the Convention, these rules will effectively lead to the abolition of all quantitative restrictions by the end of the transitional period.

The problem of the relationship of the rules adopted by the Seven concerning the abolition of quotas with the rules of the G.A.T.T. is also raised by the safeguard clause concerning balance-of-payments difficulties.

C. Definition of Origin

The most difficult technical problem in a free trade area is the definition of the origin of goods. The only goods which are free of customs duties on passing from one country in the area to another are goods which originate within the area. Goods coming from one member which did not originate within the area continue to be subject to customs duties on entering the territory of another member, just as if they came from a third country. It must therefore be possible to distinguish products which originate within the area from
those which do not, otherwise so-called deflections of trade would result. In distinguishing goods which originate within the area from those that do not, there are, in the first place, two simple cases:

1) goods coming from outside passing from one to another country in the area unchanged. There is no doubt here: these goods do not originate within the area;

2) goods completely manufactured within the area from raw materials produced within the area. There is equally no doubt here: they originate within the area.

The more difficult, and more frequent, case is where the goods are manufactured within the area from raw materials or parts which originate outside the area, or which contain certain elements which originate outside the area. In these cases the problem of the definition of origin is particularly acute. The principle adopted by the Seven is that a product of this sort is to be considered as originating within the Area when the value added within the Area to the raw materials or parts imported from outside is at least equal to a given percentage of the total value of the product concerned. This is the "added-value criterion."

The fixing of a minimum percentage of added value constitutes in a sense an acceptance of the idea that the effect on the value of the finished product of the differences between the duties levied on its constituent raw materials—because they entered the area through a member country with a high tariff rather than a low one or vice versa—gradually decreases as the amount of transformation within the area increases. If the minimum added value required to qualify a product as of area origin were too low, some diversion of commercial activity could result. In fact, it would be profitable to establish transformation industries in those countries which apply the lowest tariffs on raw materials and assembly parts. If this happened, such industries would be competing with their counterparts in countries which apply higher tariffs on raw materials and parts under artificially created economic conditions.

Because this is true, the minimum added value required to combat disparities between the tariffs of the members on raw materials and parts coming from outside should be calculated in each case on the basis of the amount of tariff disparity and the degree of work done within the area. The higher the tariff disparity, the greater amount of work would have to be done within the area in order that a finished product could be considered as originating within it. Con-
versely, the smaller the disparity, the smaller the amount of work which should be required.

With a view to simplification, the Seven adopted as a general rule the criterion whereby a product is considered as originating within the Area when 50 percent of its final value (on the basis of the f.o.b., or the free-at-frontier, price) results from transformation operations carried out within the Area.

The smaller the disparity between the national tariffs of the members on a particular raw material, the smaller should be the amount of work required to qualify the product as of area origin. If tariffs of the various countries on a given raw material are the same, a customs union rather than a free trade area exists and a very slight transformation, adding only a very low percentage to the product’s value, would be enough to qualify the product as of area origin. The same result may be reached if it is agreed that, whether their true origin be internal or external, raw materials to which the members of the area apply an identical or a very similar external tariff are to be considered as originating within the area when they are incorporated in a product manufactured within the area. For this reason the Seven also established a list of basic materials which, whatever their true origin, would be considered as originating within the area for purposes of determining whether finished goods, of which such basic materials are constituent parts, qualify for customs exemptions in passing from one E.F.T.A. country to another. In addition, certain transformation processes effected within the Area are considered to add sufficiently to the value of the material imported so that the resulting product may automatically qualify as of Area origin. For example, the spinning and weaving of wool imported from outside the Area will confer Area origin, since spinning and weaving produce cloth with a value which is more than double the price of the imported wool which it comprises.

The Seven consider that these rules concerning added value should be as liberal as possible. With this in mind, they decided to review periodically these rules in a liberal spirit, and that in any case a member of the Area may on its own initiative apply more liberal rules than those agreed to in regard to imports from the other countries of the Area.

Clearly, the more liberal the rules, the greater the number of products which may circulate freely within the Area. For European countries which are comparatively poor in raw materials, the liberal-
ity of the rules and the establishment of as broad a list of basic materials as possible are particularly important.

Once rules of origin have been established, the problem of supervising their application arises. Such supervision requires a certain number of formalities—for example, showing customs officials documents of origin—but to avoid hindering commerce within the area these formalities must be kept at a minimum. The Seven have decided that it is up to the exporter to prove that the product originates within the Area and he may do so by means of any of the above criteria.

Despite all precautions, deflections of trade or commercial activity caused by disparities between the external tariffs of the countries of the Area are still possible. To control these the Seven have further provided:

1) A “code of good conduct,” by the terms of which members promise to abstain from any step which might have as a principal effect a deflection of trade. For example, they may not deliberately undertake a systematic lowering of their tariffs as against the rest of the world in order to put their industries in a more favorable competitive position than those of the other members.

2) An appeal procedure whereby a country suffering from serious deflections of trade because of tariff disparities may submit its case to the E.F.T.A. Council. The latter may make recommendations to the other members with a view to remedying the causes of such deflections. In such cases, the rules of origin could be modified and made less liberal, but other remedies could be adapted.

D. SAFEGUARD CLAUSES

As did the Six, the Seven have created two categories of safeguard clauses, one relating to difficulties in balance of payments, and the other relating to difficulties arising in particular sectors of the economy.

I. DIFFICULTIES IN THE BALANCE OF PAYMENTS

Recourse to the E.E.C. safeguard clause is subject to a complex procedure designed to permit strict supervision of such action of a country in difficulty (in theory, except in urgent cases such recourse must first be authorized by Community institutions), to render such recourse as rare as possible and to stress the solidarity of the Six by making “mutual assistance” available. The corresponding clause
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adopted by the Seven is infinitely more flexible. Indeed the Convention provides:

1. . . . any Member State may, consistently with its other international obligations, introduce quantitative restrictions on imports for the purpose of safeguarding its balance of payments. [Emphasis added.]

2. Any Member State taking measures in accordance with paragraph 1 of this Article shall notify them to the Council, if possible before they come into force. The Council shall examine the situation and keep it under review and may at any time by majority vote, make recommendations designed to moderate any damaging effect of these restrictions or to assist the Member State concerned to overcome its difficulties. If the balance of payments difficulties persist for more than 18 months and the measures applied seriously disturb the operation of the Association, the Council shall examine the situation and may, taking into account the interests of all Member States, by majority decision, devise special procedures to attenuate or compensate for the effect of such measures.

3. A Member State which has taken measures in accordance with paragraph 1 of this Article shall have regard to its obligation to resume the full application of Article 10 [i.e., the Article requiring the elimination of quantitative import restrictions] and shall, as soon as its balance of payments situation improves, make proposals to the Council on the way in which this should be done. The Council, if it is not satisfied that these proposals are adequate, may, by majority vote, recommend to the Member State alternative arrangements to the same end.

Admittedly these provisions incorporate notions identical with those in the Rome Treaty; for example, aid of the members to a partner in difficulties. But they are presented in a less systematic and less obligatory form than in the E.E.C. Treaty. Moreover, and this is important, in the Association recourse to the safeguard clause is unilateral, the member in difficulties being obliged only to give prior warning to the others if possible. Finally, whereas in the Rome Treaty the Community institutions determine the measures that the country having difficulties may take to protect itself, methods of application, and the like, in the Association each country has complete freedom of choice, subject only to its other international obligations.

The reference to other international obligations is important. The other international organizations concerned are, of course, the I.M.F., the G.A.T.T. and the O.E.E.C. They maintain relatively
strict control over the measures taken by a country in balance-of-payments difficulties, such measures consisting of the imposition of quantitative restrictions which are to be administered in a non-discriminatory manner. Two of these organizations, the I.M.F. and the O.E.E.C., also practice what the Six in their Treaty call "mutual assistance"; the I.M.F. may grant credits and the O.E.E.C. can also appropriate credits (through the intermediary of the European Fund of the European Monetary Agreement), as well as recommend to its members measures for facilitating the import by them of the exports of the country having difficulties. In addition, both the I.M.F. and the O.E.E.C. may recommend to the country in difficulties internal financial measures (cutting back public expenditures, restriction of credit, modification of discount rates, and the like) which will enable it to regain equilibrium in its economy. They may condition the granting of credits on the institution of a plan to stabilize the country's economy. Finally, the O.E.E.C. may even go so far as to fix the time limits within which the country, which has had to re-establish quantitative restrictions on its imports because of its balance-of-payments difficulties, is again to liberate imports.

In view of this existing framework the Seven thought it useless to make special arrangements for the Association. In so deciding they had certain things in mind.

1) They wanted to manifest their desires to respect their other international obligations, and in no way to use quantitative restrictions to create a preferential regime amongst themselves.

2) The Seven wanted further to show their desire to continue to cooperate with the Six, within the framework of the other international organizations, and in particular of that of the O.E.E.C. In fact, it is this organization which has worked out the most detailed rules concerning safeguard clauses for balance-of-payments difficulties. Since 1948 these rules have functioned well, thanks to constantly strengthened examination and control procedures, to procedures permitting systematic review of the interrelationship of the economic and financial policies of its members which in turn permit preventive examination of possible balance-of-payments difficulties, and appropriate measures of cooperation to be recommended; and thanks finally to the existence, first of all, of the European Payments Union and later of the European Fund, which on several occasions permitted the appropriation of substantial credits to countries in difficulties. Since the Association of the Seven has as its aim the establishment of a broad association uniting, within the O.E.E.C.,
the Seven, the Six, and the underdeveloped countries of the O.E.E.C., the Seven thought it natural to base themselves, as concerns balance-of-payments difficulties, on the system of cooperation already tested in the O.E.E.C.;

3) Finally the Seven wanted to avoid the need for new international arrangements, since, in their opinion, those of the O.E.E.C. will normally suffice to cover both their own needs and those of the larger association of the eighteen countries of the O.E.E.C. which they hope to see formed.

Although their answer to the problem of restrictions imposed to counter balance-of-payments difficulties relies essentially on the other international institutions, the Seven were nonetheless forced to consider the possibility that protective measures of one of them might be maintained, despite the rules of the other institutions, over a long period of time. Such measures, if long maintained, could seriously disturb the functioning of the Association, and the Seven therefore concluded that E.F.T.A. institutions should supervise their application. They concede that it may become necessary, in the light of experience, to work out special procedures to attenuate or counteract the effect of these protective measures, although it is clearly impossible to foresee at present what such procedures might be. Nonetheless the gradual development of the Association of the Seven will obviously bring about an ever closer solidarity and interdependence among the members and their economies.

2. DIFFICULTIES ARISING IN A PARTICULAR SECTOR

Although the clause concerning balance-of-payments difficulties in the E.F.T.A. is more flexible than the comparable clause in the E.E.C. Treaty, the E.F.T.A. Convention clause concerning difficulties of a particular economic sector is both more complete and more rigid than its E.E.C. counterpart. This is largely because the Six decided to leave to the institutions of the Community—and in particular to the Commission—a very large measure of discretion in this field; since the E.F.T.A. will be institutionally much less centralized and less supranational, the Seven, on the other hand, wanted to establish precise rules at the outset in order to avoid giving their institutions too much discretionary power. They found, however, that there are limitations on the precision with which such rules can be defined.

In the first place a definition of this kind of difficulty was necessary. The Six refer simply to "serious difficulties which are likely to
persist in any sector of economic activity or difficulties which may seriously impair the economic situation in any region.” The Seven were more precise, the relevant clause providing:

1. If, in the territory of a Member State,
   (a) an appreciable rise in unemployment in a particular sector of industry or region is caused by a substantial decrease in internal demand for a domestic product, and
   (b) this decrease in demand is due to an increase in imports from the territory of other Member States as a result of the progressive elimination of duties, charges and quantitative restrictions . . . ,

that Member State may, notwithstanding any other provisions of this Convention,

(i) limit those imports by means of quantitative restrictions to a rate not less than the rate of such imports during any period of twelve months which ended within twelve months of the date on which the restrictions come into force; the restrictions shall not be continued for a period longer than eighteen months, unless the Council, by majority decision, authorises their continuance for such further period and on such conditions as the Council considers appropriate; and

(ii) take such measures, either instead of or in addition to restriction of imports in accordance with sub-paragraph (i) of this paragraph, as the Council may, by majority decision, authorise.

2. In applying measures in accordance with paragraph 1 of this Article, a Member State shall give like treatment to imports from the territory of all Member States.

If the country concerned is to take protective measures, the harm caused must take the form of substantial unemployment, and a spectacular fall in domestic demand, resulting from an increase in imports from the other member countries, must be the proven cause of such employment.

The Seven, it should be noted, defined the kind of protective measures that a member country may apply, and the duration of their application. The Six, on the other hand, gave the Commission full discretion.

It is interesting to observe here that recourse to the clause, in the Association of the Seven, is unilateral, whereas in the Community
it is subject to prior authorization by the institutions. Nevertheless, to limit possible abuses, the Seven were forced to limit the duration of protective measures. They also provided that, beyond the 18-month period, protective measures may be continued only with the approval of the Council. This point is important, for it implies the possibility of active intervention by the institutions of the Association. In effect, the other countries of the group, or a majority of them, must consent to continued protection by the country concerned of the sector or the region in difficulties. Thus even the Seven, who are hostile in principle to supranationality and excessive institutional intervention, were forced to envisage fairly strict institutional control in this area.

In the same vein, the Seven provided that:

3. A Member State applying restrictions . . . shall notify them to the Council, if possible before they come into force. The Council may at any time consider those restrictions and may, by majority vote, make recommendations designed to moderate any damaging effect of those restrictions or to assist the Member State concerned to overcome its difficulties.

4. If at any time after 1st July, 1960, a Member State considers that the application of sub-paragraph (a) of paragraph 2 of Article 3 [i.e., the prescribed reduction in tariffs] and paragraph 3 of Article 6 [i.e., the prescribed elimination of protective elements in internal charges and revenue duties] to any product would lead to the situation described in paragraph 1 of this Article, it may propose to the Council an alternative rate of reduction of the import duty or protective element concerned. If the Council finds that the proposal is justified, it may, by majority decision, authorise that Member State to apply an alternative rate of reduction, provided that the obligations relating to the final elimination of the import duty or protective element . . . are fulfilled.

At the same time that they make unilateral action by the country concerned possible, these measures indicate the Seven's intention that the institutions should, wherever possible, intervene before such action is taken, and the further intention that the countries of the Association should grant aid to one another to overcome difficulties. But the institutions of the Association will also be able to authorize measures other than quotas to protect a sector or a region in difficulties, or to permit it to adapt itself to external competition—for example, by subsidizing production.
In the Seven as in the Six, the safeguard clause concerning balance-of-payments difficulties is valid after the end of the transitional period as well as during that period. Moreover, and again like the Six, the Seven provided that the safeguard clause concerning particular difficulties would only be applicable during the transitional period. The Seven did, however, provide that before the end of this period the Council will consider whether similar arrangements may be thereafter necessary.

E. Conclusions

As things stand it is difficult to guess at the consequences of the creation of the E.F.T.A. The rules determining origin will not be finally defined for some time to come, and it is quite probable that they will be in a constant state of evolution during the transitional period and even, no doubt, thereafter. That definition is, of course, fundamental, for it will determine the real substance of the Area, that is to say, the volume of products, in relation to total trade between the member countries, which is to benefit from customs exemptions when passing from one country in the Area to another.

In the view of its promoters the E.F.T.A. is not, moreover, an end in itself. It is essentially a means of "thawing" the situation created by the suspension of negotiations for the establishment of a large area including the European Economic Community and the other countries of the O.E.E.C. No one can guess whether the desire of the Seven to resume talks with the Six will be realized or not. But the future of the E.F.T.A. obviously depends on whether or not the eighteen countries establish this larger association.

This being said, the most interesting question is obviously whether a free trade area is, as such, a viable concept. In the course of the negotiations in the O.E.E.C. for the establishment of a larger area, the viability of such an enterprise was fiercely attacked, particularly by France. Later, the then Finance Minister of France, M. Pinay, declared that in his opinion the free trade area was an artificial concept, illogical and completely incapable of working. It will be interesting to see whether the Seven can show that it is technically possible to make a free trade area work. Verification of origin, and the formalities this necessitates, will make commerce among the members of the Association even more difficult than at present, despite the removal of quotas and customs duties. Clearly the major preoccupation of the Seven must now be to reduce these formalities as much as possible.
The experience of the Seven in regard to deflections of activities will be equally interesting. In its present form the E.F.T.A. groups together the United Kingdom, a world commercial power which produces about everything that modern techniques make possible and which applies, in general, quite high tariffs, and six small countries, mostly with low tariffs, each of which has attained an extremely high degree of productivity. On the one hand, there is a risk that the United Kingdom will have a quasi-monopolistic position within the Area for certain products since she will enjoy customs immunity in the other six, whereas her great world competitors (the United States, Germany) will continue to pay customs duties however low. On the other hand, the United Kingdom will suffer both from her high customs duties towards the rest of the world and, in certain sectors, from the extremely active competition of her partners in the Area; and she will no longer be able to protect herself by customs duties on products in relation to which the competitive strength of her partners is greatest—for example, on aluminum, special steels, clocks and paper. Will deflections of activity within the area occur to the detriment of the United Kingdom? Or will the latter gradually achieve pre-eminence over her partners, thereby creating an ever more monopolistic situation? It is impossible to foresee what will happen without making detailed studies, sector by sector; and such studies will be made more difficult by the uncertainty, which will persist for a long time, concerning the development of the commercial policy of the countries of the Area towards the rest of the world.

Whereas it was possible to give extensive consideration to the external commercial policy of the European Economic Community, the problem of the external commercial policy of the E.F.T.A. must be passed over in silence, since, by definition, it has none, each country reserving the liberty to determine as it sees fit its commercial, tariff and quota policy, subject to its other international obligations.

The E.F.T.A. undoubtedly involves preferences among its members as to tariffs, but these are acceptable to the G.A.T.T. Third countries are nonetheless protected to a certain extent against the consequences of the creation of the Association:

1) by the fact that no member of the Association if it wants to achieve increased protection vis-à-vis the rest of the world, can do so except within the framework of its international obligations (G.A.T.T., O.E.E.C.);

2) by the declared intention of the Seven not to use quotas as a means of establishing a preferential regime among themselves. The
manner in which they have handled the problem of the safeguard clause in the case of balance-of-payments difficulties is interesting and reassuring;

3) by the underlying possibility of competition in the progressive lowering of customs tariffs that the Seven may well provoke among themselves to avoid deflections of trade or industrial activity. The fact that a country like the United Kingdom is going to find itself, without any tariff protection, in competition with the very specialized industries of low-tariff countries like Sweden, Norway or Switzerland, will naturally compel it to increase its competitive strength so that it may lower its own tariff vis-à-vis the rest of the world.

Above all, like the European Economic Community, the E.F.T.A. aims at stimulating competition among its members, eliminating marginal activities, increasing productivity and production, raising the standard of living of its population and increasing consumption. The more the competitive power of its members increases, the less they will have to use administrative measures to protect their industries. They will also no doubt be motivated to reduce tariffs slowly as the E.E.C. is to do. In this sense, without being accused of undue optimism, one might say that the movement set off in Europe within the framework of the E.E.C. and within that of the E.F.T.A. may stimulate a new movement along the road towards freedom of world trade. During the transitional periods, third countries may well believe that their interests are being harmed. It is almost certain, however, that, given a state of reasonable financial stability in which cooperation between the great powers is an essential factor, a new era of increased prosperity will open to the countries of the Western world. Their responsibilities towards the underdeveloped countries will increase correspondingly.

These general observations may now appear somewhat arbitrary. And it will only be possible to verify their validity by experience. In this respect, the measures which the Six, and the Seven adopt in regard to tariff matters and the manner in which these measures are applied towards third countries are and will be instructive, as will be the extent of cooperation in the G.A.T.T. negotiations concerning the Dillon proposal.