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NATIONAL TREATMENT OBLIGATIONS
AND NON-TARIFF BARRIERS

John H. Jackson*

INTRODUCTION

For most of the world, International Trade is governed — or guided if "governed" is too strong a term — by a complex set of international treaties and institutions centering on the General Agreement on Tariffs and Trade ("GATT"). This set of treaties and institutions (there are more than 150 treaty instruments) is part of a broader structure sometimes called the "Bretton Woods System," an arrangement put in place at the end of World War II, partly by the Bretton Woods Conference of 1944, and followed up by a series of conferences and negotiations in the late 1940s. The GATT itself was never intended to become what it is now. Instead, the countries involved in structuring the post World War II economic system originally prepared a draft charter for an International Trade Organization ("ITO"). This was completed at the Havana Conference in 1948. The GATT (as part of the ITO system) was intended merely to be a reciprocal agreement for the mutual reduction of tariffs. As is generally well known, the ITO failed to come into existence largely because the United States Congress refused to approve the Havana Charter. As a consequence, the GATT itself had to fill the vacuum, and has evolved into the principal international trade organization of the non-communist world.2

The GATT contains a number of obligations, some of which have been further elaborated through separate treaty instruments often called "codes." A principal obligation of the GATT is the "tariff binding" which sets a maximum tariff rate for massive lists of products, accepted in "tariff schedules" by each of the Contracting Parties

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(member nations) to GATT. Over the 40 year history of GATT, there have been seven major trade negotiating rounds, mostly concerned with negotiating the tariff bindings. In September 1986, a major new (the eighth) trade negotiation was launched by the GATT at Punta del Este, Uruguay, and that negotiation is now "in full stride."

In addition to the tariff bindings, the GATT has a number of rules concerning the way nation members can apply their regulations for governing trade which crosses their borders. Two GATT articles in particular deal with principles of "nondiscrimination." One of these, article I, is the famous "MFN — Most Favored Nation" clause, essentially a principle of nondiscrimination as among nations of GATT.3 The other, article III, is the "National Treatment" article, which calls for the principle of nondiscrimination to be applied as between goods imported into a GATT member and goods produced domestically within that GATT member. In this article, we will explore the second of these two nondiscrimination principles — namely, the rules and obligations of "national treatment" in the context of GATT and some of its "side codes".

The national treatment obligation is one of the most important and also one of the most contentious of the GATT trading system. It has the potential of affecting a large number of internal regulations and government measures in any country, thus treading on national sovereignty and sensitivities, ranging from the way a country governs its environment protection, consumer protection, food and drug measures, safety measures, to tax laws, etc. Consequently, it is not surprising that the national treatment obligation has been the subject of a large number of contentious dispute cases (handled under a special procedure in GATT described in other works).4

This article explores the national treatment obligation of GATT, explains some of its difficult applications, and analyzes how the obligation has been affected by some of the agreements completed in the Tokyo Round of negotiations (1973-1979).

I. THE POLICIES AND HISTORY OF THE NATIONAL TREATMENT OBLIGATION

Whereas MFN requires equal treatment among different nations,


the national treatment obligation requires the treatment of imported goods (once they have cleared customs and border procedures) to be no worse than for domestically produced goods. Obviously an important policy behind this rule is to prevent domestic tax and regulatory policies from being used as a protectionist measure that would defeat the purpose of tariff bindings. It should be noted, however, that this obligation applies to all products, not just to bound products. Thus, this rule assists the general goal of reducing restraints on imports.

A "national treatment" obligation can be found in many treaties, some dating back to earlier centuries. The scope of the obligation may vary from treaty to treaty, however, and may apply to various activities, not only to products. For example, a common application of national treatment obligations is to criminal procedures when used for foreign citizens. Another example is national treatment obligations for the "right of establishment," so that a foreign business can set up branches and offices in another country.

The national treatment obligation is often a source of complaint or dispute among nations. Since it refers to domestic regulatory and tax measures, it is intimately related to various governmental measures which are based on legitimate policy reasons not necessarily designed for purposes of restraining imports. In some cases the domestic measures will overreach or be shaped to restrain imports significantly and unnecessarily. In other cases, legitimate policy goals — including those mentioned in the article on General Exceptions to GATT (Article XX) — will prevent a measure from being inconsistent with GATT obligations. The temptation of legislators and other government officials to shape regulatory or tax measures so as to favor domestic prod-


7. The right of establishment is a critical concern with respect to the provision of services (although it may be important with respect to trade in goods). As such, the right of establishment is an important issue in the service negotiations in the Uruguay Round. See J. Aronson & P. Cowhey, Trade in Services: A Case for Open Markets 25-26 (1984).

8. Our rough calculations indicate that of the 233 disputes formally brought to GATT, 31 concern Article III. See list of some of these disputes in R. Hudec, The GATT Legal System and World Trade Diplomacy 275 (1975); J. Jackson supra note 2, at §§ 12.3-12.4; J. Jackson & W. Davey, supra note 5, at 486-96.

ucts seems to be very great, and proposals to do this are constantly suggested.10 This clash of policies raises the broader issue of whether a "harmonization" or "interface" approach is to be preferred.11

II. THE CONTOURS AND APPLICATION OF THE GATT OBLIGATION

Article III of GATT sets out the national treatment obligation pertaining to treatment of imported products. The first paragraph is a general statement of policy but includes an important phrase obligating Contracting Parties to refrain from using taxes or regulations "so as to afford protection to domestic production."12

The second paragraph of Article III requires that internal taxes on imported products shall not be in excess of those applied to domestic goods, and expressly refers to the general goal of paragraph 1. The fourth paragraph of this article imposes essentially the same obligation with respect to regulations and other "requirements affecting . . . [the] internal sale . . ." of imported products. Paragraphs 5 and 7 prohibit the use of mixing requirements to favor domestic products. Other paragraphs, however, provide some exceptions to the general national treatment rule, the most notable of which is the exception for government purchases.13

A 1958 dispute panel report involving Italian government measures relating to the sale of tractors provides a fundamental interpretation for the national treatment clause. In this case the United Kingdom complained about an Italian banking measure that provided more favorable loans to farmers buying domestically made tractors than to farmers buying imported tractors. The panel report, accepted by the Contracting Parties,14 stated, "... the intent of the drafters was to provide equal conditions of competition once goods had been cleared through customs. . . ." and particularly stressed the fact that "... the assistance by the State was not given to producers but to the purchasers of agricultural machinery. . . ."15

Thus, once the imported goods have entered the internal stream of

10. The Treaty of Rome establishing the European Economic Community has a parallel provision to GATT Article III:2 (Article 95), and this is one of the more frequently invoked provisions of the Treaty in cases before the European Court of Justice.
12. See J. JACKSON, supra note 2, at § 12.3; see also J. JACKSON & W. DAVEY, supra note 5, at §§ 8.1-8.2.
13. For a discussion of this issue, see infra section VI. GOVERNMENT PROCUREMENT.
15. Id. at para. 5.
commerce, no government regulatory measure should assist the purchase of the domestic goods without likewise doing the same for imported goods. Even though the domestic producer could be subsidized under the GATT rules (including an explicit exception for such subsidy in paragraph 8a of Article III of GATT), when the subsidy had the effect of directly influencing the purchaser's choice, it was inconsistent with the GATT.

The problem of "domestic content" rules has been troublesome. As a condition of certain regulatory or license permissions such as might be required in order to build a new factory or invest in a country, some nations have required formal or informal commitments that products produced in the new plant or assembled from imported parts be comprised of a certain minimum percent of domestic "value added." The United States brought a complaint against the Canadian government "FIRA" legislation (Foreign Investment Review Act) partly on these grounds, arguing a violation of GATT Article III.4 and 5. The U.S. argued that the necessity of a commitment to the purchase of Canadian goods where "competitively available" or otherwise from Canadian suppliers as a requirement for investing in Canada infringed GATT Article III.4. The Panel report in 1984 supported this view even when the requirement was "informal."16

A separate complaint was made by the Canadians against a United States law, known as "Section 337," and practice under it.17 This law provides a procedure whereby an American industry can complain about "unfair trade practices" of foreign parties shipping goods to the U.S. market. These practices might be infringement of copyright or patents, attempts to monopolize, etc. The Canadians alleged that the Section 337 procedure, when compared to similar U.S. domestic procedures for attacking unfair trade practices (through the FTC, Federal Trade Commission, or through patent or copyright domestic procedures), in effect discriminated against imports. A 1983 GATT Panel report concluded18 that GATT Article XX general exceptions, which allowed "necessary" differences in treatment of imports in order to secure compliance with patent, copyright, and certain other laws, was applicable. The report then went on to determine whether the 337 measures were either a "disguised restriction on international trade" or an "arbitrary or unjustifiable discrimination" and concluded that

17. See the author's forthcoming book, § 10.7.
they were neither. The report, however, did not give the Section 337 an entirely clean bill of health, noting that, in cases with different facts, it could not exclude the possibility that "there might be cases... where a procedure before a United States court might provide... an equally satisfactory and effective remedy. . . ." 

In an action brought under the so-called "New Commercial Policy Instrument," Akzo, a Dutch supplier of high-technology fibers, complained to the European Commission concerning a section 337 ban requested by the U.S. company DuPont. The section 337 action alleged infringement by Akzo of patents held in the U.S. by DuPont. The EC brought a GATT Panel proceeding arguing that Section 337 subjected imported goods to a separate and distinct procedure by virtue of their non-U.S. origin. Further, they argued, such discrimination could not be justified as "necessary" under Article XX(d) of the GATT. As of mid-1988 the panel had not reported.

III. De Facto or Implicit Discrimination

One of the more difficult conceptual problems of GATT rules is the application of the national treatment obligation in the context of a national regulation or tax which on its face appears to be non-discriminatory, but because of various circumstances of the market place or otherwise, has the effect of tilting the scales against the imported products. As sophistication about GATT rules has increased among various national officials, the number of these "implicit discrimination" cases seems to increase.

A classic example of this situation occurred in U.S. taxation of alcoholic beverages. A U.S. law (predating GATT and therefore benefiting from grandfather rights) provided for a tax of $10.50 on "each proof gallon or wine gallon when below proof." This taxing phrase applied to domestically produced alcoholic beverages as well as imported ones. A wine gallon is simply a gallon of the beverage, no matter how dilute the alcohol. A "proof gallon," however, is a gallon of liquid which is 100 proof or 50% alcohol by volume. If a producer can have his liquid taxed while at full proof, then later when the liquid is diluted to the percent of alcohol used in the beverage sold at retail (e.g., 86 proof or 43% for certain whiskies) the effective tax per gallon of liquid sold at retail is $9.03, rather than $10.50. Domestic producers were able to achieve this. Their concentrated whisky was kept in

cask under bond, and tax was paid on that basis. Only after the tax was assessed was the liquid diluted and bottled for retail sale. Importers, however, preferred to import the whisky bottled at their home place of production, and the tax was assessed at the time of importation at the wine gallon rate, thus effectively costing more per retail bottle. The importer could import the concentrated beverage, but then could not advertise “bottled in Scotland.” Also the bottling process might be more expensive in the U.S.

In several interesting cases, foreign producers challenged this U.S. tax law as a violation of certain bilateral treaties. Since the U.S. law was “grandfathered” under GATT, the GATT language was not directly involved. A U.S. court held that, since the tax law applied equally to domestic and imported products, the national treatment clauses of the treaty was not violated. However, that clause did not have the language found in GATT Article III paragraph 1 prohibiting taxes arranged “so as to afford protection.” Partly because of this language, under the GATT it can be strongly argued that even though a tax (or regulation) appears on its face to be non-discriminatory, if it has an effect of affording protection, and this effect is not essential to the valid regulatory purpose (as suggested in Article XX), then such tax or regulation is inconsistent with GATT obligations.

This brings to mind a number of hypothetical or not-so-hypothetical measures. One type of taxing proposal that has been considered is structured as follows. A uniform “excise” or sales tax (or value added tax) is imposed on the sale of a product (e.g., automobiles) whether domestic or imported. Then the company paying this tax is allowed to credit the amount paid against U.S. employment taxes it would otherwise have paid on behalf of its employees (such as social security taxes). Again, on its face, the provision appears neutral. Only when we learn that importers have very little liability for U.S. employment taxes, and thus have little opportunity to use these “credits,” do we see that the effect can be essentially discriminatory.

As another example, suppose a nation’s tax laws provide for accelerated depreciation deduction allowances for capital purchases when

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22. In Schieffelin, the treaties involved were the Ireland-U.S. Treaty of Friendship, Commerce and Navigation of 1950, and the British-U.S. Treaty of Friendship, Commerce and Navigation of 1815. The Customs Court had accepted that the British imports were entitled under the MFN clause in the British treaty to whatever tax treatment was required with respect to imports of Irish origin.

23. As observed by the author.
the materials or machinery purchased are produced domestically, but not when they are imported. It appears clear that this is even explicit discrimination. But suppose the law instead provides that the deduction is allowed only when the goods are made by persons who are paid more than an average of $25,000 per year. Again, it is clear that this is not a very well disguised discrimination. The GATT obligation does not allow for differential treatment based on characteristics of the production process, rather than the product itself.\footnote{See Belgian Family Allowances (Allocations Familiales), Report of the Panel, GATT, BISD, 1 Supp. 59 (1953). Belgian law imposed a charge on foreign goods purchased by public bodies when these goods originated in a country whose system of family allowances did not meet certain requirements. The Panel noted that this discrimination was inconsistent with the provisions of Article I "and possibly with those of Article III, paragraph 2." See R. HUDEC, supra note 8, ch. 13.}

A more subtle case is where a regulation for standardization or safety is used to effectively discriminate against imports.\footnote{For a discussion of this situation, see infra section V. TECHNICAL STANDARDS AND THE TOKYO ROUND CODE.}

**IV. BORDER TAX ADJUSTMENTS**

One of the more perplexing trade policy problems, related to the national treatment obligation but also to several other GATT obligations, is the subject of "border tax adjustments" ("BTAs"). Under GATT, a nation may charge upon importation a tax (in addition to other tariffs) equivalent to a like internal tax imposed on domestic products of the same type. As to trade in the opposite direction (i.e., exports) a nation is allowed to rebate the amount of any internal tax imposed on the exported goods. Thus, in theory, the goods travel in international trade "untaxed," and are taxed at their destination under whatever rules apply there to domestic goods as well as imported. It sounds equitable and reasonable, but these measures have been the source of considerable acrimony in international trade relations, and were considered by the United States Supreme Court in one of the few cases in which the Court has ever entertained an international trade issue.\footnote{See Zenith Radio Corp. v. United States, 437 U.S. 443 (1978); see also J. JACKSON & W. DAVEY supra note 5, 140-42.}

First, it is useful to examine the legal structure of GATT which provides for the measures described in the preceding paragraph. The language calling for this treatment is sprinkled through a number of GATT clauses. On the import side, Article II, paragraph 2(a), grants an exception from the rule limiting border charges to the amount of the scheduled tariff binding, for "a charge equivalent to an internal tax
imposed consistently with the provisions of paragraph 2 of Article III . . ." It is important to note that both Article III, and the remainder of this language of Article II, refers to taxes on products.

On the export side, matters are a bit more complex. An interpretative note\(^{27}\) to Article XVI paragraph 4 states that a rebate of internal taxes on products shall not be considered a "subsidy" for purposes of the obligation against export subsidies. In addition, a clause in Article VI likewise states that such a product tax rebate shall not be the basis of either an anti-dumping duty nor a countervailing duty in the country of import. Again one can note that the taxes involved are those on products.

These product taxes (such as a sales tax, excise tax, or tax on a product at each stage of production) are often called "indirect taxes" to contrast them from income or corporate taxes or other taxes imposed on a firm (not a product). The latter are, thus, often termed "direct taxes." Although an argument might possibly be made to the contrary, the value added taxes, such as those used in the European Community, have for a long time been considered in GATT to be "indirect" (i.e., taxes on products) and thus eligible for border tax adjustment treatment. Since these taxes are often as much as 20 percent or more, this obviously has considerable potential effect on imports and exports when border adjustments are applied.

In countries which do not generally have significant "product taxes" but instead rely much more heavily on income taxes for their revenue (as the United States does), border tax adjustments are either not used or are relatively insignificant. Income or "direct" taxes are not eligible for border tax adjustment, and this has been the source of considerable criticism by United States political and business leaders who see this disparity of treatment as unfair to their country.\(^{28}\) What is (or was) the rationale for this special approach of GATT towards border tax adjustments? At the time these rules were drafted, there probably was not too much thought given to their potential impact in

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The exemption of an exported product from duties or taxes borne by the like product when destined for domestic consumption, or the remission of such duties or taxes in amounts not in excess of those which have accrued, shall not be deemed to be a subsidy.

28. For example, section 1101(b) (16) of the 1988 Trade Act (Omnibus Trade and Competitiveness Act of 1988, Pub. L. 100-418) states that a principal negotiating objective of the United States in the Uruguay Round regarding border taxes is:
to obtain a revision of the GATT with respect to the treatment of border adjustments for internal taxes to redress the disadvantages to countries relying primarily for revenue on direct taxes rather than indirect taxes.

See also EXECUTIVE BRANCH FOR SENATE COMM. ON FINANCE, 93D CONG., 1ST SESS., TAX ADJUSTMENTS IN INTERNATIONAL TRADE: GATT PROVISIONS AND EEC PRACTICES 1. (Comm. Print 1973).
the future, since at that time tariffs themselves were relatively much more important. The BTA question, like so many others involving non-tariff measures, was in early GATT years not the focus of much attention. As tariffs declined, however, these alternative methods of affecting trade flows have become much more significant.

One theory supporting the BTA system is that taxes on products (indirect taxes) tend to be effectively borne by the purchaser or consumer of those products. It is thus said that such a tax burden is “shifted forward” to the purchaser or is a “destination” approach. In contrast, it was thought that income or “direct” taxes were born primarily by the suppliers of capital investment (i.e., are shifted “backward”) or are “origin” based. Thus it seemed fair to impose the product taxes at the destination on a basis equal to that imposed there on like domestic products. Certainly domestic producers in the country of import would perceive unfairness if the imported products were not taxed equally to their products.

To leave the products subject to the product taxes of the exporting country, however, would mean that products moving in international trade would be double-taxed — once at the place of production and again at the place of purchase or consumption. Thus it was felt necessary to exclude the products from the product taxes of the exporting countries by allowing a rebate of those taxes if necessary.

The problem, as any economist can demonstrate, is that both types of taxes have some burden on both the purchaser and the provider of capital, depending often on particular characteristics of the market structure. For example, if competition is keen, a product tax may mean that a producer will find it necessary to charge less than otherwise (to partly offset the tax effect on purchasing demand). In such a case, profitability will be lowered, and thus the return to capital is less — i.e., investors bear part of the burden of the tax. Likewise, an income tax affects the net after-tax return to capital and induces (if the market permits) the producer to charge a higher price to purchasers so as to offset the income tax effect on net profit. Thus the purchaser bears part of the burden of the income tax. There is no simple way to find the dividing line or to know the percentage of each type of tax borne by the various participants for any particular product. The division probably differs from product to product.29 Some economic com-

29. See generally, Penner, Uncertainty and the Short-Run Shifting of the Corporate Tax, 19 OXFORD ECON. PAPERS 99 (1967); J. BALLENTINE, EQUITY, EFFICIENCY AND THE U.S. CORPORATION INCOME TAX (1980); Goulder, Shoven & Whalley, Domestic Tax Policy and the Foreign Sector Formulations to Result from a General Equilibrium Tax Analysis Model, in BEHAVIORAL SIMULATION METHODS IN TAX POLICY ANALYSIS 333-64 (Feldstein ed. 1983); O. BROWNLEE, TAXING THE INCOME FORM U.S. CORPORATION INVESTMENTS ABROAD (1980);
ment suggests that even for a corporate tax up to 20% of the burden is shifted forward to the consumer in the short run, and as much as 60-75% will be shifted forward eventually. Good evidence of this (if it exists) would provide substantial arguments that income taxes should receive some border tax adjustment treatment also. Without such treatment for income taxes, those countries which depend much more on such taxes argue that goods from countries with substantial border tax rebates have not shouldered their share of the costs of government, and therefore are in essence subsidized.

How can this problem be resolved? There seems to be no good way. First of all, it is very unlikely that the GATT will be changed. Even if it could be changed, it is hard to state a rule that would be more accurate. Perhaps the present rule is as good a rough approximation of equity as can be found, and it is at least administrable. In a floating exchange rate world, at least where the product taxes are generally uniformly applied to all products, it can be argued that the exchange rate adjusts to any border tax adjustment so that over a few years (at least), most distortion effects of the BTA are neutralized. Another approach for the "income tax" nations is to shift to a value added or product tax for a much larger portion of revenue and then to utilize a border tax adjustment. To change an otherwise desirable tax system to try to achieve some uncertain and perhaps dubious advantage for the international trade seems much like the "tail wagging the dog." However, if such a product tax system has other merit to commend it, it does not hurt that a by-product might be some less concern about perceptions of unfairness of the international trade rules.\(^{30}\)

The issue of "pass-through" of indirect taxes was raised in a recent case before the Court of International Trade\(^ {31}\) in which a U.S. producer challenged, \textit{inter alia}, the assumption of the Commerce Department that an indirect tax would be completely passed through to the eventual purchaser. Commerce argued that it knew of "no reasonable method" for accurately measuring the incidence of a tax. The C.I.T. rejected this approach stating that "a conclusion that full pass through occurred in all cases is not supported by substantial evidence" and remanded back to Commerce. In a later administrative review\(^ {32}\),


\(^{32}\) Television Receivers from Japan; Final Results of an Anti-dumping Duty Administrative
Commerce continued to work on the assumption that full pass through occurred, and stated that the government was considering an appeal against the decision of the C.I.T. However, as neither side wished to proceed any further, the case was never brought.

V. TECHNICAL STANDARDS AND THE TOKYO ROUND CODE

Implicit discrimination against imports is often found in the context of so-called "product standards." Examples are numerous. A nation which utilizes metric measures for tools and small fasteners might require all such products to be marked in metric measures. There may be a valid domestic consumer protection policy supporting such a requirement, but it might also be introduced because troublesome import competition stems from products which are marked in other measures, such as inches or feet. Likewise, in one case it was said that a Pacific-Rim nation required packages of food products to be in its own language and no other. While there seems to be ample policy grounds to require the labels to have the language of the country of import, to require that no other language occur on the label is to prevent the use of a cost-saving multi-lingual label.

Sometimes it is alleged that agencies or industry groups which set standards consciously try to "gerrymander" those standards to make it comparatively more difficult for foreign producers to comply. In such a way a market for electronic components might be protected for domestic producers by certain quality or standards specifications. Likewise drug or cosmetic standards might be "shaped" to allow domestic manufacturers to accommodate them easily.

The process of obtaining clearance of a product subject to inspec-
tion for health or safety reasons may also add enough of a burden to the importation of goods as to “afford protection” to domestic manufacturers. Even though the country of export may test and examine goods which are exported, the importing country might require this to be done again. In some cases it may have good reason to do this. The exporting nation’s tests may be unreliable or may not require as high a standard as that of the importing nation. If the exporting nation’s tests are specifically for exports (and not domestically consumed products also), that nation may not have a strong incentive to provide stringent testing, in contrast to the nation whose consumers will purchase the good. On the other hand, delay and costs of processing tests in the importing nation, whether due to under-staffing of the testing agency, or a tacit understanding by that agency that “slowness helps the balance of trade,” clearly goes contrary to the liberal trading policies of the international system.

Much of the controversy and, indeed, anger about Japan’s apparent unwillingness to import centers on practices such as those just mentioned. The Japanese government has responded with various programs designed to prevent such measures from inhibiting imports and to mute the criticism leveled at Japan for these measures.  

Because of the risk that these various problems will become increasing sources of protectionism and of conflict, the GATT Contracting Parties negotiated in the Tokyo Round a new code designed to address these questions. This “Agreement on Technical Barriers to Trade” essentially reiterates the GATT Article III obligations, stating,

Parties shall ensure that technical regulations and standards are not prepared, adopted or applied with a view to creating obstacles to international trade. Furthermore, products imported from the territory of any Party shall be accorded treatment no less favorable than that accorded to like products of national origin and to like products originating in any other country in relation to such technical regulations or standards. They shall likewise ensure that neither technical regulations nor stan-


standards themselves nor their application have the effect of creating unnecessary obstacles to international trade.

Beyond this general “national treatment” type obligation, there are few substantive rules in this Tokyo Round code, but the agreement specifies a number of obligations regarding the procedure by which product standards are developed in each of the signatory nations. Under the Code, governments must to the extent possible (recognizing that many product standards are developed by non-government groups) ensure that foreign nations and their producers with an interest in exporting shall have the opportunity to be heard and to present facts and arguments to standards making bodies during the formulation of standards. In addition the Code calls for “transparency” of standards — that is, adequate notice and opportunity to comply. It urges the development of international standards and urges parties to recognize testing which has been appropriately done in the country exporting products.

Some consider this Code to be one of the more successful results of the Tokyo Round since it has the largest number of acceptances of any of the codes (33, including both developing and non-market economies). Its operation in practice, and the activity of its Committee of Signatories, seems to have engendered satisfaction among governments and businesses. At least one dispute brought formally under this Code’s dispute settlement mechanism has been satisfactorily resolved.

Our discussion here has centered on the standards for products themselves. Another important problem is that of standards, relating not to the product itself but to the manufacture or processing of the products and their impact on the pollution of the environment and the safety of workers.

VI. GOVERNMENT PROCUREMENT

The most important exception to the national treatment obligation in GATT Article III itself is found in paragraph 8 relating to government procurement. The language provides some interpretative difficu


38. See the author’s forthcoming book (particularly § 9.4).
culties but generally makes exempt from Article III national treatment obligations the purchases by "governmental agencies of products purchased for governmental purposes." Since the Article I MFN obligation of GATT makes reference to the obligations of Article III, paragraphs 2 and 4, it may be argued that government procurement is also an exception to MFN rules.

Early preparatory drafts of the ITO charter and GATT would have included government procurement in the discipline of those instruments. However, government negotiators objected, so the final drafts included explicit exclusions. Apparently government procurement was too closely tied to sovereignty to permit regulation at that time. Since military procurement would have been exempted in any event, the drafters worried that any attempt to draw lines between exempt and included government procurement would be too difficult.

There are several important reasons why this exception had become very troublesome by the 1970's. First, there had been some trend of increasing the government sector of a number of economies, so that in some nations over 40 percent of gross national product would pass through government budgets. Where major industry sectors, such as steel or utilities, were nationalized, an increasing amount of economic activity was beyond the reach of the GATT rules. U.S. manufacturers of heavy electrical equipment (such as turbines) saw great exporting potential if foreign restrictions on government purchases of imports could be softened. The problem of non-market economies could potentially be even more troublesome in this regard.

A second important (and related) reason for concern was the difficulty of finding an agreed definition of either "government agency" or "governmental purposes." Nations have a wide variety of ideas as to what is the appropriate sphere of government activity. In some countries it is automatically assumed that the government should own and run railways, telephone systems, all electricity generation, travel bu-

39. GATT, Art. III:8, BISD vol. 4 (1969). For example, para. 8(a) used the phrase "products purchased for governmental purposes." The question of what is a "governmental purpose" can be very troublesome indeed. See, for an American example, Bethlehem Steel Corp. v. Board of Commissioners, 276 Cal. App. 2d 221, 80 Cal. Rptr. 800 (1969).


reasus, airlines, and many other activities which private enterprise conducts elsewhere. Some countries have added to the list basic "smokestack" industries including steel and coal as well as major related service sectors such as banking. Such an important exception from the GATT trading rules would clearly diminish the liberalizing effects of those rules.

Thus it was that another code which came out of the Tokyo Round was the "Agreement on Government Procurement." This Code is interesting because of the apparent far-reaching rules included in it. The general rule is stated as in Article II, paragraph 1, as follows:43

With respect to all laws, regulations, procedures and practices regarding government procurement covered by this Agreement, the Parties shall provide immediately and unconditionally to the products and suppliers of other Parties offering products originating within the customs territories (including free zones) of the Parties, treatment no less favourable than: (a) that accorded to domestic products and suppliers; and (b) that accorded to products and suppliers of any other Party.

The Code outlines detailed rules to implement this general principle, including rules governing the bidding procedures to be followed. These regulate the type of technical specifications which can be required in bids: tendering procedures including public announcement, qualification of bidders, time-limits, tender documents, etc. Foreign bidders are entitled to obtain a statement of reasons why their bids were rejected, and a dispute settlement mechanism is established to follow through on complaints. Several cases have already been processed through this procedure.44

Although the Code requirements may seem far-reaching, the important limitation of the Code is that it only applies to the governmental "entities" on a list appended to the Code for each signatory. The scheme has characteristics very similar to that of tariff bindings in GATT. As part of a process of reciprocal negotiation among the Code signers, each country specifies by name to which entities the Code applies. The basic goal of the draftsmen was to have the Code establish a framework for truly effective discipline against governmental discriminatory purchasing, recognizing that such stringent requirements would make governments somewhat hesitant to include entities on


their list. Once the Code came into existence, with reciprocal negotiated lists of entities, later negotiations were contemplated for additions of more entities to the list. Some later negotiations have been held, and more are contemplated.

The scope and coverage of the Government Procurement Agreement additionally depends on certain other clauses in it. Although it explicitly applies (interestingly enough) to most "services incidental to the supply of products," a minimum threshold for covered contracts was set at "SDR 150,000." An exception was also provided for national security and, in a qualified way, for national measures to protect public morals, order, safety, health, and similar goals.

As of mid-1988, 13 nations have accepted this agreement, and it has been reported that in 1983 over $38 billion worth of trade was covered by it. Telecommunications has been a large issue in connection with the agreement, and this issue has figured prominently between the United States and Japan. In the U.S. telecommunications has not been government owned, and even its monopoly power has been diluted by the trend to "deregulation." Thus, the U.S. argues that foreign suppliers have the opportunity to sell telecommunication equipment in the U.S. market. On the other hand, most other nations have a government-owned telecommunications monopoly, although several have recently decided to "privatize" or deregulate also. From the end of the Tokyo Round onward, the U.S. and Japan have negotiated strenuously over U.S. demands that U.S. companies have better opportunities to sell products to the Japanese telephone monopoly. From the U.S. perspective, these negotiations have had only moderate success. On the other hand, in at least one case, the Japanese demonstrated that a U.S. telephone company, AT & T, refused a purchase of Japanese equipment (which was the low bid in a competition) for "Buy American" reasons.

46. SDR 150,000 was approximately $149,000 in 1986. This threshold amount has subsequently been lowered to SDR 130,000 (GATT, BISD 33 Supp. 190 (1987)), which for 1988 had a dollar value of $156,000.
49. In 1981 Fujitsu submitted a bid to supply fiber optic cable to AT&T. When AT&T considered accepting the bid, which AT&T freely admitted was the lowest, Congressman Timothy Wirth wrote to the FCC pointing out the national security implications of such a purchase. Wall St. J., Oct. 19, 1981, at 26, col. 3; N.Y. Times, Dec. 11, 1981, at D1, col. 6. AT&T later rejected Fujitsu’s bid and decided in favor of Western Electric, the manufacturing arm of AT&T. N.Y. Times, Jan. 18, 1983, at D4, col. 5. However in 1982, MCI awarded a similar contract to Fujitsu. Wall St. J., June 18, 1982, at 12, col. 3.
In the United States, there are many "Buy American" regulations, both at the federal and at the state level. A 1979 International Trade Commission study found some twenty-five instances of regulatory preferences for U.S. goods at the federal level alone. The United States is not unique in requiring preferences for domestically-produced goods. However, it is unusual in legislating such preferences.

The best example is the Buy American Act, which essentially requires acquisition of domestically produced articles for "public use." In an important exception, the law authorizes the federal authorities to deviate from this rule if the cost of foreign-produced articles is lower by specified amounts.

Although federal procurement policies now limit Buy American provisions in order to open government markets in accordance with the MTN Agreement, state Buy American statutes have proliferated in recent years. Thirty-six states now have some form of Buy American legislation, compared with twenty-three a decade ago. Interestingly enough, the United States was prepared to accept the Code as applicable to governmental subdivisions, but other nations were actively opposed, so this remains an exception to the international code.

52. E. McGOVERN, supra note 40, at 213-19.
54. The President has set this cost difference at 6%. 48 C.F.R. § 25.105.
55. J. JACKSON, J. LOUIS & M. MATSUBHITA, supra note 33, at 200-01.