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Consequences of the present situation for the common agricultural policy

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I. INTRODUCTION

1. The crisis currently affecting the world's monetary, financial and trade relations has causes which go deeper than those linked to the present economic situation. In international economic relations there exists an almost permanent tendency towards disequilibrium and instability. This is due to the considerable difference in size between the US economy, which, through the key role played by the dollar, is capable of transmitting to the rest of the world its own possibly disruptive impulses, and the economies—much smaller in size—of other countries whose economic policy in general and balance-of-payments objectives in particular, tend to lack coherence when confronted with one another or with those of the United States.

2. This disequilibrium increased progressively during 1970-1971 following the accelerated growth in the United States deficit, itself due in part to a deterioration in the American basic balance (current transactions and long-term capital movements), but mainly caused by speculative movements in the form of massive outflows of American capital and the influx of international funds into the European markets. The considerable amount of international liquidity available, especially on Euro-currency markets, has greatly accentuated the disruptive trends brought about by the deterioration in the basic American position.

3. On 15 august 1971 the United States Government decided to introduce an important batch of measures to reflate the economy while avoiding any aggravation of the speculative pressures bearing on the dollar. These measures concern:

(a) The exchange system and the status of the dollar

(i) dollar convertibility into gold and other reserve assets was suspended;

(ii) The US Administration stated its intention to obtain changes in the exchange relations between the dollar and other currencies and to bring about a reform of the international monetary system, with a view particularly to making it more flexible.

(b) Trade policy

A 10% temporary import surcharge was introduced from 16 August 1971. It is applied to all dutiable goods (i.e. especially to manufactures); at the same time, various other measures were taken or announced, the details

of which will be given elsewhere in this document, and whose object is to strengthen the competitive position of American products and to increase income generally whilst reducing spending abroad.

(c) *Reflating the economy and limiting the effects of certain inflationary factors*

(i) An accelerated programme for the reduction of personal income tax, originally planned for 1973, is to be implemented;

(ii) A request was made to Congress to remove the tax on purchases of cars (on average this means a price reduction per car of about $200);

(iii) It is planned to cut federal spending by $4 700 million. A 90-day price, wage and rents freeze was decreed;

(iv) Foreign aid was reduced by 10%.

4. According to the statements made by President Nixon and the American representatives at GATT and in the Group of Ten, the aim of these measures is a spectacular turnabout in the American balance-of-payments position. The improvement is expected to be of the ordrer of $13 000 million. In the absence of precise and definite information as to the exact significance of this figure, it may be compared with certain orders of magnitude which can be worked out from the following headings, the amounts of which, as an annual trend, would be representative of the United States balance of payments towards the middle of 1971:

(in $ '000 million)

1. Trade balance	— 1.5
2. Services account	+ 0.5
3. Balance of non-monetary capital movements	— 8
4. Net outflow of non-recorded capital and other errors and omissions	— 5
5. Overall balance to be financed (1 to 3)	— 14

The hoped—for turn—about seems to be expected mainly from restoring a surplus on the trade balance similar to that enjoyed at the beginning of the sixties. The suppression of speculative capital movements—referred to under "errors and omissions"—would also help appreciably in achieving the desired result.

The very size of the planned turnabout indicates that powerful measures will have to be used if the economic policy defined by the Administration on 15 August is to bear fruit rapidly.

5. The American decision to change the position of the dollar was followed by considerable disruption on stock exchanges and in exchange relations. The international rules imposing strict limits on currency fluctuations, which in preceding months had been successively flouted by Canada, then Germany and the Netherlands, have now *de facto* been suspended or adapted by the world's leading nations. The International Monetary Fund is unable to carry out in orderly fashion the transactions for which it is responsible, all kinds of difficulties are making themselves felt in the operation of international markets and a tendency towards compartmentation has reappeared in international payments.

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II. CONSEQUENCES ON THE ECONOMIC ACTIVITY AND THE WORKING OF THE COMMUNITY

Such, briefly, is the general situation whose effects on the Community's economic activity and the working of its policies and institutions must now be assessed.

A. Overall economic assessment

Any attempt to assess the measures taken by the United States Administration must necessarily be based, at the present time, on simplified assumptions and must allow for the time required for these measures to achieve their full effect.

The automatic effect of the Administration's measures and the modifications which have already occurred in exchange relations will tend to reduce the balance on the Community's trade account with the rest of the world by about 2 000 million units of account and cut the rate of growth of its exports to non-member countries—at present of the order of 8%—by 3 to 4 points. The effects of these measures will vary considerably from industry to industry as regards the speed and extent to which they are felt and their duration. It is, therefore, difficult at the present time to assess them globally in terms of growth or jobs. It may be feared already, however, that they will introduce an element of uncertainty into the Community's economic development.

Moreover, in the absence of recent statistical information, the effect of the current situation on capital movements in the EEC can hardly be assessed except in respect of short-term capital. The influx of the latter seems generally to have been stemmed following the *de facto* adaptation of exchange rates, the strengthening of direct controls or simultaneous application of both these procedures.

As regards long-term capital movements between the United States and Europe, it is probable that initially at least the combined effect of the depreciation of the dollar in terms of revalued currencies, discrimination in the United States in favour of home-produced machinery and equipment and possible other measures, will tend to reduce the amount of direct investment from the United States, particularly since the depreciation of the dollar will increase the cost of buildings and equipment abroad. As regards investment in stocks and shares, there could be an incentive for Europeans to purchase these if there were a lasting recovery on the New York Stock Exchange. Purchases by American residents of European securities will continue to be adversely affected by the interest equalization tax, the incidence of which will be accentuated by the increased dollar price of foreign shares.

On the whole, although the impact of the present situation does not seem to have been very marked so far, several threats will still hang over the European economy in the next few months. The pressure on European countries to revalue their currencies might well push exchange rates beyond the tolerable limit from the angle of the level of economic activity and employment; the repercussions of the United States' trade measures will progressively develop their dampening effects, while continued uncertainty in monetary matters will have an increasing effect on international transactions, both commercial and financial.

B. Direct and indirect consequences for the Community's economy and social situation

The measures taken or envisaged by the United States in the trade field, either together with the strictly monetary measures or in isolation, are likely to affect the Community's trading position and thus the level of activity in the main industries concerned.

The 10% surcharge on imports affects about 87% of the Community's exports to the United States, i.e. about $5 735 million, or 12.8% of total EEC exports in 1970. The Community in fact exports few products admitted into the United States at zero duty or subject to quantitative restrictions, and which are thus exempt from the surcharge. The effect of the surcharge will be roughly to double the average incidence of the American tariff, thus wiping out most of the concessions obtained through careful balancing operations in the Dillon and Kennedy Rounds. Since most raw materials, imported at zero duty, are exempt from this surcharge, the latter will increase the effective protection accorded to value added by processing within the United States.

In absolute money terms, the main industries likely to be affected are:

Motor vehicles	$1 450 million
Machinery	$1 030 million
Iron and steel	$ 620 million
Textile and clothing (non-cotton)	$ 370 million
Footwear	$ 310 million
Chemicals	$ 270 million
Scientific, cinematographic, photographic and optical equipment, clocks and watches	$ 230 million
Manufactured metal goods	$ 170 million
Beverages	$ 140 million

Certain industries (footwear, cars, glass, diamonds, tyres) are specially geared to the American market, but for some of them the effect of the surcharge will not amount to 10% because of the "buffer" constituted by the 1930 tariff.[1] The surcharge on cars, for example, will amount to only 6.5%.

The actual figures for the exports affected by the surcharge are given, sector by sector, in Annex 3 together with their percentage in relation to EEC exports.

For the time being the effects of the differences in exchange rates must be added to those resulting from the surcharge. It will be permissible to pass on the exact amount of surcharge to selling prices as long as the price freeze continues in the United States, but not the increases caused by depreciation of the dollar in relation to other currencies.

If endorsed by Congress, the 10% Job Development Tax Credit, reserved for goods produced in the United States, will have a particularly striking effect on capital goods, since it will be cumulative with the surcharge and the *de facto* revaluation of certain currencies. It is likely to triple, or even quadruple, the protection granted to the competing American product, and capital goods represent a large part of the Community's exports to the United States.

The effects of the American measures on the Community's exports will therefore probably be very considerable where capital goods are concerned. The repercussions for consumer goods in general and semi-finished products will depend to a large extent on the exporter's ability to reduce his profit margin or to incorporate some or all of the surcharge in his selling prices without thus losing his market. In the short term it must also be remembered that contingency reserves are held in the United States as a precaution against strikes or threats of strikes in different industries (such as steel) or in certain ports. Methods of customs valuation (the American Selling Price), protectionist pressures in certain industries and various non-tariff obstacles may also play a role.

When considering Community imports, it must be borne in mind that the measures taken or planned by the United States will increase the competitiveness of their exports. The plan for a Domestic International Sales Corporation (DISC), if voted by Congress, will constitute a direct export subsidy in the form of direct tax rebate.[2] The tax credit for new investment, whether discriminatory or not vis-à-vis imported materials, will have the effect of stimulating productivity growth.

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[1] See Annex 1, p. 20.
[2] The Administration estimates that it will increase exports by about $ 1 500 million per annum.

The freezing of wages in the United States while they will probably continue to rise in the Community will strengthen the American competitive position. When considering these various measures it should also be pointed out that only 60% to 70% of United States productive capacity is at present being used, and that the measures to reflate the economy will have the effect of increasing the productivity of American industry.

In the short term, any changes in traditional trade relations are unlikely to be very great. Exports from countries strongly geared to the American market should to a large extent remain constant. The *de facto* revaluation of the yen means that Japanese industry, which obtains most of its raw materials from abroad, will see its supply costs diminish. Moreover, its lower cost prices, compared with the industries of the other industrialized countries, make it seem likely that it will be able to absorb the surcharge and remain competitive in its main export industries (cars, steel, electronic consumer goods). Canada will probably take certain measures to offset the effects of the surcharge, at least partially.

In the medium and long term, the US measures may, however, lead to a diversification of export flows from the industrialized countries which, until now, were largely orientated towards the American market. Japan, for example, is likely to place greater emphasis on penetrating Asian and European markets.

The Community's exports to non-member countries other than the United States may also be affected by increased competition in certain sectors from America and from certain other non-member countries.

The effects on the Community's imports and its exports to non-member countries are difficult to assess, particularly because of the uncertainties concerning monetary movements. Only after some months will it be possible to see how Community trade is shaping.

The considerable growth in external trade over the last few years may, however, be expected to slow down.

The repercussions — direct or indirect — of the US measures are likely to affect in varying degrees the different sectors of the Community's activity. In most cases, they would only be felt in a few months if the monetary uncertainties and the American measures were to last. They would then be all the greater if they were to be combined with some slowing down in production due both to present anti-inflation policies and to postponement of investments caused by economic or monetary uncertainties.

Certain goods and certain companies may however feel the effects of the American measures more sharply, either because they are specially orientated towards the American market, or because they will be more exposed to competition from non-member countries. This could lead to problems which

would be both regional, because of the location of the companies most affected, and social through the likelihood of unemployment and reductions in working hours in these firms.

To these effects may be added, as regards intra-Community trade, the effects of currency floating, which is not compatible with a single market, since it leads to a worsening of the competitive position of those Member States whose currencies have appreciated in relation to the others, except where agricultural products covered by compensatory measures are concerned.

Furthermore, currency floating has created imbalances between the Community's frontier regions. It exerts a direct influence on the income of wage-earners in these regions who are tempted to go and work in the neighbouring country where the currency has increased in value. The region could in this way lose an increasing number of workers and local companies could be faced with recruitment problems, especially for qualified staff. This situation could have consequences on the efforts of the state in question to develop or reconvert these regions.

C. Effects on the working of Community machinery

Before the announcement of the American measures, the disorder on financial markets and the steps taken by different Member States had already led to difficulties in operating Community machinery. The events of August increased these difficulties.

The most worrying effects were felt in the field of the common agricultural policy and especially its common organization of the markets. The consequences will be dealt with in a special report from the Commission in response to the Council's request at its meeting of 13 September 1971.

However, the major consequence of the monetary situation on the institutional system of the common agricultural policy is that, since currency floating is incompatible with the application of a single market in farm products, the Community has been obliged to waive this principle temporarily and to introduce compensatory amounts (import taxes, export subsidies) for the main products.

Although the introduction of this system was inevitable if the common agricultural policy was to be operated in the short term, these measures are nonetheless obstacles to intra-Community trade and involve frontier checks. They also represent a step backwards along the road to achieving a single market between Member States, and make the management and future development of the common agricultural policy more arduous. Their negative effects will make themselves increasingly felt the longer they are applied.

It is still not possible to assess accurately the economic consequences of these measures on intra-Community trade and trade with non-member countries. Certain negative effects are already being felt and, in the longer term, it is to be feared that grave repercussions will appear.

In its relations with the Member States and economic transactors the Community, as an entity with rights and obligations, faces problems entailed by the diversity of its national currencies and the risks of possible exchange rate variations. It has tried to solve these difficulties by using the method of the unit of account. If the latter is to fulfil effectively the role expected of it, the amounts expressed in this unit must be convertible into national currencies —this being the only method of payment—at rates which may be accurately fixed in advance or automatically adjusted. If these conditions are not fulfilled, the relationship between income and expenditure may be jeopardized.

Thus, the commitments and payments of the European Development Fund are calculated in units of account and the nature of its transactions is such that, generally, a considerable time lapses between the date when the commitment is made and when payment takes place, so that, as things now stand, there is no guarantee that a particular commitment will be sufficient to cover the corresponding expenditure in a floating (revalued) currency.

Furthermore, most transactions financed by the Fund give rise to international contracts following a call for tender, so that it is impossible to know in advance the currency in which the payment will be made. No anticipatory measures may, therefore, be taken except at the risk of immobilizing large amounts of credits to no profit.

This may have consequences for resources of the EDF also, since practically all its payments on behalf of the AASM are in Community currencies or currencies linked to these, and since its endownment is fixed in units of account. Ability to achieve its aims therefore depends on the exchange value of these units in Community currencies.

It would be premature at this stage to try to assess the repercussions of the floating of certain currencies and, more generally, of the monetary situation on the Fund's potential.

The Commission already feels that the Community should pay particular attention to this question at the appropriate time.

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The various difficulties may be temporarily neutralized by means of special measures or palliatives of an administrative and accounting nature. This, however, leads to a tissue of provisions which are so many obstacles to the smooth running of the Community and its institutions, and whose injurious effect in the more or less long term should be taken seriously.

III. REPERCUSSIONS OF THE AMERICAN MEASURES ON DEVELOPMENT AID

1. Repercussions on the flow of aid to the developing countries

The 10% reduction in American public aid means a 3% to 4% reduction in total aid to developing countries from member countries of the DAC and may further threaten the goal of allocating to the developing countries at least 1% of the industrialized countries' GNP, 0.7% of which is to be in the form of public aid.

The United States' bilateral commitments in 1970 to Africa south of the Sahara, which showed a slight increase over those of earlier years, amounted to about $224 million, of which about 55 million were allocated to the AASM. Assuming a linear reduction in American aid, the "loss" to the AASM may be calculated at between $5 and 6 million per annum. The Ivory Coast and the Democratic Republic of the Congo, the main beneficiaries, will be the countries most affected.

Following these cut-backs in aid, requests from some of the AASM and developing countries to the Community or the Member States for increases or a revision of their aid programmes, cannot be excluded.

2. Repercussions on the trade of the AASM and other developing countries

The surcharge on American imports affects approximately 12% of the AASM's exports to the United States (see Annex 4). The countries most affected are Madagascar, a third of whose exports have to face additional import duties, the Democratic Republic of the Congo (18%) and Ivory Coast (7%).

In Madagascar, the most important products hit by the American measures are vanilla and cinnamon, exports of which to the United States reached $8.1 million and 1.1 respectively in 1969.

Certain other Asian and Latin American developing countries which have reached a higher degree of industrialization than the AASM, are likely to suffer harm as a result of the American measures, especially for a number of manufactured and semi-finished products.

3. Generalized preferences

There is now much less chance of seeing the United States implement its system of generalized preferences on behalf of the developing countries in the near future. From this angle the speech made by the US representative

to the UNCTAD Trade and Development Board at its 11th session at the end of August, is particularly significant: "When the American measures were announced, no decision had been taken as to the date on which the Bill on generalized preferences would be submitted to Congress. The Administration is moving with caution so as not to jeopardize the chances of obtaining the approval of Congress."

A considerable delay in implementing legislation on generalized preferences by the United States would not fail to affect the distribution of the burden amongst the donor countries, both those like the EEC, which granted the preferences on 1 July, and others which have already introduced them, such as Japan, or plan to grant them by 1 January 1972.[1] In principle, the Community, like the other donor countries, has attached to its offer of generalized prefences a clause stipulating that it was made "on the assumption that all the main industrialized countries which are members of OECD would also grant these preferences and would make comparable efforts for their success".

However, it is only right to point out that the system of ceilings adopted by the Community shelters it from the disadvantages of an inequitable distribution of burdens which, it is hoped, will not last very long. It is rather the Community's Associates who might be at a disadvantage in a situation of this kind, since it would deprive them of some of the compensations they were entitled to expect in sharing their preferences on the Community market.

At the most recent meeting of the Association Council in April 1971 these countries had stressed the dangers of the Community implementing its system of generalized preferences before the other donor countries did likewise and before a balanced distribution of burdens between all donor countries had been achieved.

4. Untying of aid to the developing countries

The DAC draft agreement on untying aid seems, for political reasons, if not definitively in jeopardy, at least destined to be shelved for the time being, as is clear from the request not to include this item on the agenda of the next top-level DAC meeting, scheduled for October. In the present situation, it is hard to imagine the United States, which strongly supported the untying of a large share of bilateral and multilateral aid, opening their bilateral aid to international competition.

[1] These intentions were confirmed at the 11th session of the UNCTAD Board, i.e. after the American measures.

5. Conclusions

In the field of development aid the American measures may:

(i) Have an impact on the amount of aid the AASM and other developing countries might receive;

(ii) Bring up the question of the introduction by the United States and the other industrialized countries of the generalized tariff preferences on behalf of the developing countries;

(iii) Jeopardize the long-standing efforts to persuade member countries of the DAC (the OECD Development Assistance Committee) to untie a large part of the aid to developing countries.

DESCRIPTION OF THE AMERICAN MEASURES

Trade measures

A. Import surcharge

1. *Date of entry into force*

The surcharge announced on 15 August by the President of the United States came into force at 12 noon on 16 August. After an initial refusal, the United States Administration finally agreed, on 2 September, to exempt goods exported to the United States before this date, i.e. goods already under way, those stored in customs warehouses and those blocked in ports through strikes.

These exemptions did not, however, cover goods dispatched after 16 August under contracts signed before that date.

2. The surcharge is applicable to all products imported into the United States, with the exception of those non-dutiable and those subject to a statutory or semi-statutory system of quantitative import restrictions.

(a) The category of goods on which there is a zero tariff consists mainly of raw materials and tropical products such as coffee and fish. These products are mostly imported from the developing countries and Canada. Products of the Canadian automobile industry imported at zero duty will also under the bilateral agreement be exempt from the surcharge.

(b) Products subject to import quotas in the United States and thus not affected by the surcharge are, according to the Department of the Treasury regulations, crude oil and petroleum products, beef, veal and mutton, sugar, certain milk products, wheat, groundnuts, raw cotton and cotton textiles.

On the other hand, the products for which certain countries or industries have been obliged to accept limits on their exports to the United States, are not exempt.

3. *How the surcharge works*

The additional duty is usually equal to 10% *ad valorem*. It is added to existing tariffs for the products concerned, i.e. the tariff in force at 1 January 1971, the 4th stage in the Kennedy Round reductions. It also

includes a freeze on the fifth reduction scheduled for 1 January next year. However, the total duty under any tariff heading may not exceed the tariffs fixed by the 1930 Tariff Act (2nd column of the United States Tariff). Consequently, for a few headings for which the difference between the 1930 tariff and that in force before the recently announced measures was less than 10%, the surcharge will be below this rate. It will also not be imposed on the few products whose rates are still at the level of the 1930 tariff (ham and products which were subject to retaliatory measures during the "chicken war").

The 1930 tariff, still applicable to countries not enjoying most-favoured-nation treatment, was very high and appreciable reductions were made to it during later negotiations. This tariff therefore covers very sensitive products for which the reductions are less than 10 points, or products for which, in 1930, duties had been fixed at low rates. This is the case for cars (10% in 1932, 6% before the Kennedy Round, 3.5% at present), certain kinds of footwear, diamonds, tyres and motor cycles.

An analysis of the 10% surcharge shows that it does much more than cancel out the results of the Kennedy Round, since the incidence of the average American tariff has been almost doubled.

Finally, the non-application by the United States of the final stage of Kennedy Rounds reductions, on 1 January 1972, will increase the effects of the surcharge from that date.

4. *The link with the price freeze*

At the same time President Nixon decided on a 90-day price freeze, at the level of prices as they stood in the month up to 15 August 1971. This freeze will not, however, be applicable to the prices of unprocessed agricultural products.

As regards imported products:

(a) The surcharge may be fully reflected in the selling price so long as the price increase does not exceed the actual amount of the surcharge. Successive sellers must, therefore, be able to prove that surcharge has been paid.

(b) Price increases resulting from fluctuations in the world market for the product imported may also be incorporated into the selling prices so long as the product does not lose its physical identity. Once it is processed, the above price increase may no longer be passed on.

(c) The effects of fluctuating exchange rates in relation to the dollar may not be incorporated into the selling price.

5. *Possibility of discriminatory application of surcharge*

The President has given the Secretary of the Treasury the permanent power to reduce, remove or reimpose the surcharge or to provide exemptions either of an overall nature or generally for a given article or for an article imported from a given country, if he feels that such a measure would not prejudice the US balance of payments. This delegation of power constitutes a grave source of potential discrimination. The refusals to provide Canada and the developing countries with exemptions show, however, that the US Administration does not intend to make use of this power for the moment.

6. *Duration of the surcharge*

The imposition of the surcharge is announced as a temporary measure. No date has, however, been fixed for its expiry. The President explicitly linked its removal with the end of the "unfair treatment" caused by "unfair exchange rates". This statement has been interpreted by some of his assistants as meaning that the surcharge will not be lifted until the American balance of payments has reached a basically stable position.

Other statements by members of the Administration give the impression that it is intended to link a reduction or removal of the surcharge with the removal of certain obstacles which the United States claim they encounter in exports, especially of farm products, to some of their trading partners.

Mr Connally, the Secretary to the Treasury, has stated that some of the negotiations following on the measures taken by his Government would try to remove these obstacles and ensure that in the future nations operated on the same footing.

7. *Compatibility with GATT*

At the examination by the GATT working party of the US surcharge, from 6 to 10 September, all its members, except the United States, considered that:

(i) The surcharge was not in conformity with GATT rules;

(ii) It was inappropriate, given the nature of the United States balance-of-payments situation and the undue burden of adjustment placed upon the import account with consequent serious effects on the trade of other contracting parties.

The working party's conclusions are given in Annex 2.

B. Tax measures to stimulate investment

Under the heading "Job Development Tax Credit", the President asked Congress to provide exemption from direct taxation for investments in new machinery and equipment.

This measure may be defined as a tax credit to be deducted from the tax bill. It will be equal to 10% of the cost of equipment brought into service after 16 August 1971. This will be reduced to 5% after 15 August 1972. The rate for public services will be half the general rate. Special procedures are laid down for machinery with a useful life of less than 8 years: no tax credit is provided for machinery with a useful life of less than 4 years, 1/3 of the credit for between 4 and 6 years, 2/3 between 6 and 8 years. Maximum amounts are also fixed in line with the taxpayers' liabilities. These procedures are similar to those of the investment tax which was in force until 18 April 1969.

The new and important factor in trade policy is that this tax credit will not be available for purchases of machinery and equipment "predominantly" produced abroad,[1] at least so long as the import surcharge remains in force. Once the surcharge is removed, the tax credit will also be granted for imported equipment.

The tax exemption should, on the one hand, stimulate purchase of new machinery and equipment from American industry and, on the other, increase the productivity and, thereby, the competitiveness of industries which make new investments, especially export industries.

The exclusion of imported equipment from this tax relief is definitely discriminatory. The Administration has moreover not tried to hide the fact that this exclusion was decided on with the aim of creating a preference in favour of the American engineering industry which is alleged to be exposed to greater competition from abroad.

The GATT working party stated that the fact that the tax credit is not applied to import equipment is definitely contrary to Article III, which lays down that "taxes and other internal charges ... should not be applied to imported or domestic products so as to afford protection to domestic production" (§1) and that "products imported ... shall not be subject, directly or indirectly, to internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly, to like domestic products" (§2).

Several delegations pointed out that the cumulative effect of this measure, together with the surcharge and the revaluation of certain currencies would practically put an end to certain trade flows.

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[1] According to the statements made by the US representative in the GATT working party, all equipment made up of more than 50% of imported parts by value will be considered to be foreign machinery.

C. Forwarding to the American Congress of the Bill setting up a Domestic International Sales Corporation (DISC)

The DISC constitutes a preferential tax status for exporting companies whose undistributed profits will no longer be subject to company tax. This proposal had already figured in the 1970 US Trade Act which had not been adopted by the Senate at the end of that year. The United States notified GATT of its intention to ask Congress to pass this Bill, but then asserted that it was not part of President Nixon's economic measures and refused to discuss the matter.

The original proposal provided only for the full application of the tax arrangement only after 1974. The exemption would only have been partial during a transitional period (in 1971, 50%, in 1972 and 1973, 75%). Whilst retaining the essential contents of the former Bill, the President has stated that the new one, which is to come into force on 1 January 1972, is to be applied immediately without any transitional period. Furthermore, the untaxed profits resulting from the exports of the companies in question may be used, not only for re-investment purposes in the export field, but also for financing industrial readaptation (for example, retraining of workers, conversion aids, etc.).

It is worthwhile briefly recalling the important elements of the DISC tax arrangement, which was in fact examined on 3 March 1971 by the Standing Committee of Heads of Revenue Departments from the EEC countries. The DISC Bill provides for the setting up of a new kind of corporation whose profits will be free from corporation tax so long as at least 95% of its activities are export-related. Moreover, the tax concessions granted under the DISC arrangement may even be extended to profits over and above a normal profit margin in export business, since the parent corporation, which sets up the DISC, may sell its goods to the latter at a price which will enable the DISC to make a large profit. Tax exemption on these profits remains valid during the period in which they are reinvested in the export subsidiary company or are used in the form of a loan to the parent company or to another company in the United States whose goods are exported under certain specific conditions.

The basic reason for the proposal to introduce tax benefits on behalf of DISC's is the desire to redress the US balance of current payments. This new arrangement has been referred to, moreover, as an export incentive. However, the Americans try to justify the DISC Bill by alleging that foreign companies have tax advantages as regards their exports which US companies do not enjoy.[1] According to the Commission's Departments, and the EEC

[1] and that, consequently, this tax arrangement should offer compensation to companies situated in the United States. This is also the stance adopted by the United States in its notification to GATT.

Standing Committee of Heads of Revenue Departments, the American allegations are based on false premises where the Community is concerned:

(a) It is not true that tax on company profits is heavier in the United States than in the Community. Not only do certain European countries levy heavier tax than is the case in the United States, but also the difference in the rate as between certain Member States is even greater than that existing between the United States and the Six as a whole.

(b) It is mistaken to believe that tax refunds to exporters in countries applying the value added tax system put American exporters at a disadvantage; for, with taxation on company profits not being greatly different as between the United States and the Community, full compensation of indirect tax on exports and imports cannot represent an advantage for Community companies. It should also be recalled that, according to the study of the effects of VAT on external trade carried out by the GATT Working Party on Border Tax Adjustments, this tax is not likely to be disruptive to trade relations between the United States and the Member States of the Community.

(c) Furthermore, it should be pointed out that the principle of territoriality applied by certain Member States in not taxing certain trade and industrial activities abroad is much more limited than the DISC provisions, which grant exemption for income earned at home.

The DISC tax arrangement is incompatible with Article XVI §4 of GATT, which bans any subsidy on the export of any product other than commodity, "which subsidy results in the sale of such product for export at a price lower than the comparable price charged for the like product to buyers in the domestic market".

Moreover, the United States accepted the Declaration of 19 November 1960 prohibiting subsidies on the export of any product other than commodities. The report of the Working Party which studied the measures to be taken includes a non-limitative list of measures which the governments prepared to accept the Declaration consider to be subsidies within the meaning of Article XVI §4. This list expressly mentions "exemption from direct taxation ..... granted to industrial and commercial undertakings under the head of exports."

All these arguments were expounded by the Community representative in the GATT working party.

CONCLUSIONS OF THE GATT WORKING PARTY ON THE UNITED STATES TRADE MEASURES - SURCHARGE

Geneva, 6-10 September 1971

1. The Working Party took note of the findings of the IMF and recognized that the United States had found itself in a serious balance-of-payments situation which required urgent action. While noting the contrary views of the United States, the other members of the Working Party[1] considered that the surcharge, as a trade-restrictive measure, was inappropriate given the nature of the United States balance-of-payments situation and the undue burden of adjustment placed upon the import account with consequent serious effects on the trade of other contracting parties.

2. In the spirit of Part IV of GATT, and in view of the possibilities opened up by the newly adopted generalized system of preferences, the Working Party explored with the United States the feasibility of exempting more products exported by developing countries from the surcharge. The Working Party fully understood the keen desire and the urgent need of developing countries to expand their exports as well as the importance of the United States market to them, and generally agreed that in spite of the exemption of many raw materials and primary products normally exported by them, the import surcharge significantly affected the export interest of developing countries. The Working Party wished to stress this as an *a fortiori* reason why the measure should be eliminated within a short time.

In the meantime, the United States should keep the situation under constant review so as not to overlook any possible opportunity of adding to the exemptions list products of particular export interest to developing countries.

3. The United States, taking into account the findings of the IMF, considered itself entitled under Article XII to apply quantitative restrictions to safeguard its external financial position and balance of payments but had chosen instead to apply import surcharges, which were less damaging to world trade. It noted that while a number of other contracting parties had taken similar action there was no uniform precedent in the GATT for dealing with situations of this kind.

[1] One member (Greece) reserved its position concerning the "inappropriateness" of the surcharge.

The other members of the Working Party concentrated their attention on the measures which the United States had actually adopted in this respect, and noted that the surcharge, to the extent that it raised the incidence of customs charges beyond the maximum rates bound under Article II was not compatible with the provisions of the General Agreement.

4. The Working Party noted that the surcharge, if not removed within a short time, could not but have far-reaching effects on the world economy and international trade, particularly having regard to the inhibitive effect it would have on international cooperation necessary for the continuation of the liberalizing trade policies that have been pursued since the inception of GATT.

5. The Working Party noted the statement by the United States confirming that the import surcharge would be temporary and, in the light of the above, urged that it be removed within a short time.

6. It was understood that this examination in no way prejudiced the rights of contracting parties under the General Agreement.

IMPACT OF THE AMERICAN SURCHARGE ON THE COMMUNITY'S EXPORTS

Details per industry

1970 in $ '000 000

CST	Description of product	Exports in 1970			Products exempted from surcharge			Products subject to surcharge		
		Outside EEC	To USA	US % share	Zero duty	Quant. restrictions	1930 tariff	Volume of trade	% of exports to USA	% of exports outside EEC
00	Live animals	36.6	1.4	3.8	1.0	—	—	0.4	29	1
01	Meat and meat preparations	270.6	77.4	28.6	—	—	76.2	1.2	2	0.4
02	Dairy products and eggs	459.8	35.6	7.7	—	16.0	0.3	19.3	54	4
03	Fish and fish preparations	68.0	8.1	11.9	1.7	—	0.7	5.7	70	8
04	Cereals and cereal preparations	646.3	8.7	1.3	0.6	—	0.1	8.0	92	1.2
05	Fruit and vegetables	512.6	35.1	6.8	4.2	—	0.5	30.4	87	6
06	Sugar and sugar preparations	127.6	8.0	6.3	—	0.5	—	7.5	94	6
07	Coffee, tea, cocoa, spices and manufactures thereof	156.6	43.5	27.8	9.8	5.0	—	28.7	66	18
08	Feedingstuff for animals	116.0	3.1	2.7	1.9	0.2	—	1.0	32	1

CST	Description of product	Exports in 1970			Products exempted from surcharge			Products subject to surcharge		
		Outside EEC	To USA	US % share	Zero duty	Quant. restrictions	1930 tariff	Volume of trade	% of exports to USA	% of exports outside EEC
09	Miscellaneous food preparations	98.3	4.7	4.8	—	0.3	3.4	1.0	21	1
0	*Food*	2 492,4	225.6	9	19.2	22.0	81.2	103.2	46	4
11	Beverages	493.3	140.8	28.5	—	—	2.8	138.0	98	28
12	Tobacco and tobacco manufactures	62.4	2.8	4.5	—	—	—	2.8	100	4.5
1	*Beverages and tobacco*	555.7	143.6	26	—	—	2.8	140.8	98	25
22	Oilseeds, oil nuts and oil kernels	16.0	0.9	5.6	—	—	—	0.9	100	5.6
29	Animal and vegetable crude materials, inedible n.e.s.	237.0	39.8	16.8	14.7	—	0.1	25	63	11
ex 2	*Commodities of agricultural origin*	253.0	40.7	16	14.7	—	0.1	25.9	64	10
41	Animal oils and fats	9.6	0.5	5.2	—	—	—	0.5	100	5.2
42	Vegetable oils and fats	68.0	9.9	14.5	0.9	—	—	9.0	91	13
43	Prepared oils and fats and animal or vegetable waxes	32.7	1.0	3.0	—	—	0.2	0.8	80	2.4
4	*Animal and vegetable oils and fats*	110.3	11.4	10	0.9	—	0.2	10.3	90	9
	Total for agriculture	3 411.4	421.3	12	34.8	22.0	84.3	280.2	67	8

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		Outside EEC	To USA	US % share	Zero duty	Quant. restrictions	1930 tariff	Volume of trade	% of exports to USA	% of exports outside EEC
21	Hides, skins and fur skins, undressed	69.1	5.3	7.7	4.6	—	—	0.7	13	1
23	Crude rubber	97.9	2.8	2.9	0.1	—	—	2.7	96	3
24	Wood, lumber and cork	59.5	0.5	0.8	0.1	—	—	0.4	80	1
25	Pulp and waste paper	24.5	0.3	1.2	0.3	—	—	—	—	—
26	Textile fibres and waste	344.9	22.9	6.6	5.7	—	—	16.2	76	5
27	Non-metalliferous ores	175.7	19.6	9.5	11.6	—	—	8.0	41	5
28	Ores and scrap metal	87.2	2.8	3.2	2.1	—	—	0.7	25	1
ex 2	*Industrial raw materials*	858.8	54.2	6.3	24.5	—	—	29.7	55	3
32	Coal, coke and briquettes	171.2	0.4	0.2	0.4	—	—	—	—	—
33	Petroleum and its by-products	1 461.7	118.4	8.1	2.0	109.7	—	6.7	6	0.4
34	Gas	30.4	0.4	1.3	0.4	—	—	—	—	—
3	*Energy products*	1 663.3	119.2	7.2	2.8	109.7	—	6.7	6	0.4
51	Chemical elements and compounds	1 442.7	148.6	10.3	28.3	—	—	120.3	81	8
52	Mineral tar and crude chemicals from coal, petroleum and natural gas	16.7	3.3	19.8	3.3	—	—	—	—	—

CST	Description of product	Exports in 1970			Products exempted from surcharge			Products subject to surcharge		
		Outside EEC	To USA	US % share	Zero duty	Quant. restric-tions	1930 tariff	Volume of trade	% of exports to USA	% of exports outside EEC
53	Dyeing, tanning and colouring material	495.4	31.0	6.2	—	—	—	31.0	100	6
54	Medicinal and pharmaceutical products	757.2	26.4	3.5	7.0	—	—	19.4	73	3
55	Essential oils and perfume materials, toilet, polishing and cleansing preparations	315.5	35.2	11.1	9.8	—	—	25.4	72	8
56	Fertilizers, manufactured	273.2	4.3	1.6	4.3	—	—	—	—	—
57	Explosives	27.6	1.9	6.9	—	—	—	1.9	100	7
58	Plastics	1 041.1	47.9	4.6	—	—	—	47.9	100	5
59	Chemicals n.e.s.	582.8	30.5	5.2	2.6	—	2.9	25.0	82	4
5	*Chemicals*	4 952.2	329.1	7.1	55.3	—	2.9	270.9	82	6
61	Leather, leather manufactures, and dressed furs	208.9	38.3	18.3	—	—	—	38.3	100	18
62	Rubber manufactures, n.e.s.	414.5	97.8	23.6	—	0.2	—	97.6	100	24
63	Wood and cork manufactures	148.6	18.2	12.2	0.2	—	—	18.0	99	12
64	Paper, paperboard and manufactures thereof	390.4	11.0	2.8	—	—	—	11.0	100	3

CST	Description of product	Exports in 1970			Products exempted from surcharge			Products subject to surcharge		
		Outside EEC	To USA	US % share	Zero duty	Quant. restric-tions	1930 tariff	Volume of trade	% of exports to USA	% of exports outside EEC
65	Textile yarn, fabrics, made-up articles and related products	2 168.3	316.5	14.6	5.7	58.0	—	252.8	80	12
66	Non-metallic mineral manufactures	1 177.2	274.2	23.3	15.2	—	—	259.0	94	22
67	Pig iron, iron and steel	3 320.7	624.6	18.8	0.1	—	—	624.5	100	19
68	Non-ferrous metals	928.0	136.1	14.7	13.8	—	—	122.3	90	13
69	Manufactures of metal	1 466.4	176.7	12.0	9.0	—	—	167.7	95	11
6	*Manufactured goods classified chiefly by material*	10 223.0	1 693.4	16.6	44.0	58.2	—	1 591.2	94	16
71	Machinery other than electric	8 803.3	891.0	10.1	78.7	—	—	812.3	91	9
72	Electric machinery, apparatus and appliances	3 257.1	221.6	6.8	—	—	—	221.6	100	7
73	Transport equipment	6 301.3	1 654.1	26.2	59.5	—	2.7	1 591.9	96	25
7	*Machinery and transport equipment*	18 361.7	2 766.7	15.1	138.2	—	2.7	2 625.8	95	14
81	Sanitary, plumbing, heating and lighting fixtures and fittings	137.8	17.5	12.7	—	—	—	17.5	100	13
82	Furniture and fixtures	198.3	28.3	14.3	—	—	—	28.3	100	14
83	Travel goods, handbags and similar articles	75.4	24.8	32.9	—	0.4	—	24.4	98	32

CST	Description of product	Exports in 1970			Products exempted from surcharge			Products subject to surcharge		
		Outside EEC	To USA	US % share	Zero duty	Quant. restrictions	1930 tariff	Volume of trade	% of exports to USA	% of exports outside EEC
84	Clothing	696.7	185.9	26.7	—	22.8	—	163.1	88	23
85	Footwear	549.0	314.1	57.2	—	—	—	314.1	100	57
86	Professional, scientific and controlling instruments: photographic and optical goods, watches and clocks	1 144.0	225.6	19.7	—	—	—	225.6	100	20
89	Miscellaneous manufactured articles n.e.s.	1 500.9	307.4	20.5	105.6	—	—	201.8	66	13
8	*Miscellaneous manufactured articles*	4 302.1	1 103.6	26	105.6	23.2	—	974.8	88	23
	Total for industry	40 361.1	6 066.2	15	370.4	191.1	5.6	5 499.1	91	14
9	Miscellaneous transactions and commodities n.e.s.	1 421.8	145.8	10.2	132.7	—	2.0	11.1	7.6	0.8
	Overall total	45 209.3	6 634.0[1]	14.6	537.9	213.1	91.9	5 791.1	87.2	12.8

[1] American statistics of imports from the EEC: $ 6 574 million. This slight difference does not affect the percentages.

Note: The Community's export statistics (columns 3 and 4) are taken from the tables of the Statistical Office of the European Communities (1970).
The statistics concerning products exempted from the surcharge (columns 6 to 8) are taken from United States import statistics (1970). These statistics have been adjusted so as to take account of the difference in nomenclatures.
Both series are based on fob values.
Any differences between the two series of statistics may be a result of the different ways of classifying them, since export statistics are generally less accurate than import statistics. These differences should, however, not appreciably affect the orders of magnitude and the percentages figuring in the last three columns.

IMPORTS INTO THE UNITED STATES FROM THE AASM AND OCT IN 1970

(in $ '000 000)

Country of origin	Total	Subject to customs duties	Exempt from customs duties
Mauritania	0.7	—	0.7
Cameroon	25.4	2.4	23.4
Senegal	0.8	0.6	0.1
Ivory Coast	92.2	6.6	85.6
Togo	1.3	—	1.3
Central African Republic	6,4	insignificant	6.3
Gabon	8.9	—	8.9
Congo (Kinshasa)	40.7	7.5	33.2
Burundi and Rwanda	21,2	—	21,2
Somalia	0.2	—	0,2
Madagascar	31.9	11.0	20,8
	229.7	28.1	201.7
St. Pierre and Miquelon	1.8	1.6	0.2
Netherlands Antilles	412.9	108.4	304.6
Surinam	56.1	0.9	55.3
French Pacific Islands	8.3	0.1	8.2
Territory of the Afars and Issas	0.2	—	0.2