INTERNATIONAL MONETARY FUND

Developments in the Doha Round and Selected Activities of Interest to the Fund

April 8, 2003

Contents | Page

LIST OF ACRONYMS

ACP	African, Caribbean and Pacific countries
AD	Antidumping
BIT	Bilateral Investment Treaty
CAP	Common Agricultural Policy
DDA	Doha Development Agenda
DSB	Dispute Settlement Body
EU	European Union
FDI	Foreign Direct Investment
FSAP	Financial Sector Assessment Program
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
HIPC	Heavily Indebted Poor Country
LDC	Least Developed Country
MFN	Most Favored Nation
OECD	Organization for Economic Cooperation and Development
RTA	Regional Trade Agreement
SDT	Special and Differential Treatment
TRIPS	Trade-Related Aspects of Intellectual Property Rights
VAT	Value-Added Tax
WTO	World Trade Organization

Glossary of WTO Terminology

Amber Box – trade-distorting domestic subsidies subject to reduction commitments under the Uruguay Round Agreement, such as support prices or subsidies directly related to production quantities. ***De minimis*** provisions exclude subsidies equivalent to up to 5 percent of agricultural production for developed countries, and 10 percent for developing countries, from the Amber Box.

Blue Box – direct payments under production-limitation programs, not subject to reduction commitments under the Uruguay Round Agreements.

Geographical indications – property rights to place names, such as Champagne or Emmental.

Green Box – permissible subsidies, not subject to reduction commitments. In order to qualify, Green Box subsidies must not distort trade, or at most cause minimal distortion. They have to be government-funded and must not involve price support. Green Box support includes, e.g., many forms of direct income support, environmental protection and rural development programs.

LDCs – the classification "least developed countries" refers to a subset of 49 developing countries, as defined by the United Nations (UN).

Tariff peaks – are defined as tariffs of 15 percent or higher, or about three times the average tariff level in industrial countries.

Tariff escalation – is said to exist when tariff rates rise as the level of processing of a product increases.

Bound tariff rates – represent a country's commitments in the WTO and thus are an upper bound on tariff rates.

Applied tariff rates – the rate actually imposed by customs administrations at the border.

I. Introduction

1. **The current round of multilateral trade negotiations launched by the WTO in 2001 has the potential to significantly boost global growth and welfare.** The Doha Development Agenda (DDA) provides an opportunity to update and reinforce multilateral rules, aims at liberalizing trade in effectively the whole spectrum of tradable goods and services, and broadens the scope of the WTO mandate to new areas. Key benchmarks for the talks and the main negotiating areas are listed in Annexes 1 and 2.

2. **The round is entering a critical phase in the run-up to the Cancún Ministerial meeting of the WTO (September 10–14)**. The meeting is scheduled to prepare the ground for detailed negotiations ahead of the deadline for a completion of the round by January, 2005. There have been slippages in the timetable established at Doha in negotiations on agriculture, public health provisions of the Trade-Related Aspects of Intellectual Property Rights (TRIPS) agreement, special and differential treatment (SDT) for developing countries, and "implementation issues."[1] Given the nature of the negotiations as a single undertaking, these delays are increasingly seen to affect talks in other, less contentious areas as well.

3. **With key issues unresolved, there is concern that the agenda at Cancún might become unmanageable and that ambitions for the round would be watered down.** Many have expressed doubts whether the domestic political conditions for agreement are in place in important areas, such as agriculture. Transatlantic tensions could stiffen resistance to compromise, as might the rapid spread of bilateral and regional trade initiatives, which some observers fear is eroding negotiating capacity and political interest in the multilateral approach. An unsatisfactory outcome at Cancún might prompt a less conciliatory approach to a number of outstanding trade disputes.[2] And it would send the wrong signal at a time of fragility in the world economy.

4. **On the other hand, the current negotiations are further advanced than at a comparable point during previous rounds**. The Doha timetable may have been optimistic with regard to what could be achieved in the early phase of the talks. The Round

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[1] These refer to several dozen requests by developing countries for flexibility in the implementation of the Uruguay Round agreements.

[2] These include U.S. complaints over an EU ban on beef hormones, and WTO rulings on the U.S. Foreign Sales Corporation tax law and steel safeguards, among others, all of which are being pursued with little resolve at present in order not to complicate the multilateral talks. The Uruguay Round "Peace Clause," which restrains recourse to legal proceedings in agricultural trade, expires at the end of the year. This may also entail a more confrontational approach.

might be following the pattern of previous General Agreement on Tariffs and Trade (GATT) negotiations, which required the threat of breakdown in order to mobilize political capital for sensitive decisions. The global political environment might actually help, if it is followed by efforts to mend fences. With the services negotiations already fairly advanced, agreement on the negotiating modalities for agriculture and industrial products would in fact settle much of the substance of the round. If these were agreed at Cancún, the talks would rebound.

5. **The high profile given to the development dimension of the round adds a sense of urgency.** This dimension was reinforced at Monterrey and Johannesburg and is seen as an important factor in achieving the Millennium Development Goals. The DDA aims to facilitate the fuller integration of developing countries into the global trading system, and many areas of special interest to developing countries were front-loaded in the negotiating agenda. However, the slippages on the initial deadlines relate mostly to development issues.

6. **The current difficulties may partly reflect expectations gaps at the outset of the talks.** From the start, there has been ambivalence about the limits of negotiating briefs in crucial areas, such as agriculture. Uncertainties were heightened by passage of the 2002 U.S. Farm Act and delays in the EU's mid-term review of its Common Agricultural Policy (CAP). Furthermore, there are different views on what might constitute a "development-oriented" outcome to the talks. Developing countries have expended considerable effort to obtain special treatment, reflecting the perception that development interests are better served by carve-outs from multilateral disciplines than by determined efforts at economic integration. There is also a tendency in a number of countries—developed and developing—to view preference margins as a measure of the "development value" of the round, with a focus on least developed countries (LDCs). This is being turned into an argument for limiting market access for a wider range of countries. Finally, the logic of reciprocal liberalization that has underpinned the GATT is not easily reconciled with a development orientation calling for less-than-fully-balanced concessions. Tactical considerations may have tempered the advanced economies' willingness to offer broad concessions in areas of interest to developing countries.

7. **This paper aims to take stock of the negotiations and to identify the main challenges for a successful outcome at Cancún.** The following section describes the positions and differences that have emerged in selected areas of negotiations on market access and rules. The paper then examines a number of issues that intersect with the Fund's work in the fiscal and financial areas, and that require close contacts between the Fund and the WTO in the period ahead. These include selected topics in the financial services negotiations, the discussion about an international investment framework and the fiscal implications of trade liberalization.

II. Status of Negotiations

A. Market Access Negotiations

Agriculture

8. **WTO members remain sharply divided over further reforms and liberalization of agriculture.** Draft papers on modalities for agricultural liberalization prepared by the chairman of the negotiating committee have failed to bridge the gap. The focus of agricultural exporters, primarily the United States and the Cairns Group,[3] is on substantial improvements in market access, the elimination of export subsidies and reductions in domestic supports (see Table 1). Their proposals envisage a flattening of peak tariffs—requiring high-tariff countries to make bigger cuts. The EU, Japan, and Switzerland, among others, favor proportional cuts and emphasize nontrade concerns, such as the environment, food safety, cultural factors, as well as geographical indications.[4] They also propose to subject export credits and food aid, as well as the state trading practiced by some of the Cairns Group countries, to the same disciplines as export subsidies. With regard to domestic support, there are differences over the use of so-called "Blue Box" subsidies—which the EU regards as only mildly trade-distorting but necessary to promote nontrade concerns—and the *de minimis* provisions[5] favored by the United States, but viewed as a loophole by others.

9. **For developing countries, some of the proposals envisage substantial flexibility in the pursuit of food security objectives and quota- and duty-free market access for LDCs.** The EU and the African Group, among others, argue that significant most favored nation (MFN) liberalization and the resulting erosion of tariff preferences would expose the weakest developing countries to intense competition in OECD markets, primarily from Cairns Group exporters. At the same time, opening LDC markets might subject them to price volatility and food insecurity. This has been questioned by others who view competitiveness as a supply-side problem, based on evidence that few LDCs or ACP countries have been able to take advantage of preferences to raise their exports in the past, and food security as a function of incomes rather production, as protection diminishes purchasing power and thus security.

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[3] Argentina, Australia, Bolivia, Brazil, Canada, Chile, Colombia, Costa Rica, Fiji, Guatemala, Indonesia, Malaysia, New Zealand, Paraguay, the Philippines, South Africa, Thailand, and Uruguay.

[4] Property rights to place names.

[5] These relate to minimum thresholds of support as a share of production value below which subsidies are excluded from reduction commitments.

Table 1. Summary: Market Access Negotiations—Key Negotiation Positions

Agriculture

Proposals have been received from all the major players and can be summarized as follows:

The main elements of the **EU proposal** are:

- Reducing the average tariff by 36 percent, with a minimum reduction per tariff line of 15 percent;
- Reduction in export subsidies by an average of 45 percent across different products, while accepting the phase-out of some export subsidies;
- Reductions in the "Amber Box" category of trade-distorting domestic support by 55 percent;
- The extension of the level of protection of geographical indications (GIs) in the agriculture talks, with the aim to include an index of additionally protected GIs in the Agreement on Agriculture;
- As regards developing countries, a "food security box" to facilitate the implementation of further tariff reductions and to meet the developing countries' concerns on sensitive agricultural crops.[1]

The main elements of the **U.S. and Cairns Group proposal** are:

- A formula approach to tariff cutting that would reduce all developed country agricultural tariffs to below 25 percent;
- Elimination of all forms of export subsidies phased in over a short implementation period;
- Substantial reduction, with a view to elimination, of trade-distorting domestic support. The United States proposes that domestic support should not exceed 5 percent of the value of agricultural production;
- The United States proposes that "Blue Box" trade distorting support linked to production limitations should be included in the calculation of *de minimis* limits of 5 percent of agricultural production.[2]

Other important proposals have come from different groups of **developing countries**, particularly in the area of SDT, and include the following:

- Under SDT developing countries should be allowed to draw up a positive list of products that would be subject to tariff commitments;
- A proposal for a "development box" that would capture SDT for developing countries in the Agreement on Agriculture.

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[1] The EU is proposing a special safeguard instrument for developing countries in order to ensure food security.

[2] In the current Agreement on Agriculture there are no limits on spending on "Blue Box" subsidies. The U.S. proposal to include "Blue Box" subsidies in the *de minimis* calculations will effectively reduce "Blue Box" support.

Table 1. Summary: Market Access Negotiations—Key Negotiation Positions (continued)

Industrial Goods

Detailed proposals have been received by the main players and can be summarized as follows:

- **U.S. proposal**: The elimination of duties on all industrial goods by 2015, starting from applied rates or the Uruguay Round bound rate, whichever is lower, and binding all final rates.

- **EU proposal**: The application of a formula-based mechanism for tariff reduction that would considerably reduce all industrial tariffs by compressing them into a flatter range. The compression should start from bound rates or applied rates for unbound tariffs.

Services

Services is a heterogeneous negotiating area. Key themes under consideration depend on the mode of supply and the type of service.

- **Developed countries** emphasize in particular further liberalization of rules on access, mainly through commercial presence, in important sectors and insist on the need for further market opening. Proposals published thus far indicate an interest in telecommunications, financial services, transport, business (including professional), and distribution services.

- **Developing countries** attach particular importance to the liberalization of temporary cross-border movements of natural persons and seem to be interested in market openings for professional services, tourism, audiovisual, distribution, and computer services. They also attach importance to the development of disciplines in areas such as emergency safeguards.

Financial Services

Some of the main proposals received have been from the United States, the EU, and some developing countries, such as Colombia and Korea.

- **U.S. proposal** stresses that further liberalization should be based on two pillars—verifiable benchmarks for further liberalization and transparency rules set specifically for the financial sector.

- **EU proposal** places priority on the further liberalization of rules on commercial presence in financial services trade, including the elimination of ceilings on foreign ownership in the financial sector, the authorization for foreign financial institutions to adopt the legal form of their choice, and nondiscriminatory access to the domestic payment system of the host country.

- **Developing countries** are concerned about the pace of possible future liberalization of trade in financial services, insisting that the pace of liberalization be consistent with a member's level of development. They argue that increased competition and capital mobility as a result of liberalization might destabilize their financial sectors.

10. **Developing countries, an increasingly heterogeneous group, express concerns about the proposals of all the major players.** Many point out that the EU proposal would not entail a significant improvement in market access, except for LDCs. The U.S. proposal is viewed by some countries as lopsided, as it is overly permissive of the types of support favored by the United States, while targeting those favored by others. Several contend that the U.S. and Cairns Group proposals pay insufficient attention to special and differential treatment for net food-importing developing countries and to increasing market access for LDCs.[6] Nevertheless, it is clear that developing countries—some of which are members of the Cairns Group, while others are net food importers that benefit from price-depressing OECD subsidies, and others still enjoy market access privileges in OECD markets—do not have a unified position on agriculture. Disagreement over the meaning of a "development orientation" in agriculture may complicate the search for a compromise.

11. **The March 31 deadline on agreeing modalities for the agriculture negotiations was missed.** While WTO members agreed to continue discussions, it may well be left to ministers to break the deadlock at Cancún. Securing a broadly acceptable outcome on agriculture would provide significant momentum to the entire round, as countries are delaying progress in other areas contingent on developments in the agriculture negotiations. Progress in the negotiations is partly dependent on the internal EU debate over the Mid-Term Review of the CAP. Passage of the core elements of the European Commission's proposals, including the decoupling of agricultural supports,[7] would increase the leeway of EU negotiators for concessions on both subsidies and market access. According to most observers, any compromise would also require the recognition of nontrade concerns, with protection for geographical indications perhaps first in line. At the same time, a broad consensus is unlikely to emerge, unless developing country fears over food security are addressed.

Industrial Goods

12. **The negotiations over industrial goods have been moving along well, and most observers believe that there will be convergence on negotiating modalities by May, barring negative repercussions from the agriculture talks.** Most members appear to favor the combination of a formula-based approach with bilateral request/offer reductions, starting from bound tariffs, phased in stages, and with less than full reciprocity for developing

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[6] Some developing country groups have been advocating a "development box" to capture food security needs.

[7] Decoupled support—i.e., support unrelated to price and production levels—would allow subsidies to be shifted into the "Green Box," which remains outside WTO disciplines, and reduce reliance on border protection to sustain domestic prices.

countries. Such an approach has the potential to eliminate tariff peaks and compress tariff escalation, thus improving the conditions for exports of low-technology products of particular interest to developing countries (e.g., textiles and clothing, leather products, and processed foods). As shown in Table 1, the U.S. proposal is more ambitious than those of the EU and others, but it appears that differences have narrowed.

13. **Initial developing country concerns over the depth of proposed tariff reductions have become less pronounced**. But many are now linking progress on industrial tariffs with the agriculture negotiations. The LDCs are requesting that all developed countries provide them with duty- and quota-free access to their markets under Generalized System of Preferences (GSP) schemes. More controversially, some have called on industrial countries to ensure that preference margins are not eroded by MFN tariff reductions.

Services

14. **In services, the process of exchanging bilateral requests and offers has been proceeding broadly on schedule.** Nevertheless, reflecting in part cross-linkages with the agriculture talks, offers from only a few countries had been received by the March 31 deadline. While developing countries have been more active participants than they were during the Uruguay round, this has been mostly on account of the larger middle-income countries.[8] A number of others have sought to gain acceptance for a monitoring mechanism to ensure that there is effective implementation of Article IV of the General Agreement on Trade in Services (GATS), dealing with increasing participation of developing country members in world services trade, and Article XIX.2, which contains SDT-related provisions for developing countries.[9]

15. **Some observers suggest that progress in these talks is driven by the limited overlap between sectors of primary interest to both developed and developing countries.** This is seen to provide scope for mutually beneficial compromises. However, it is difficult to assess the nature of the bargains being struck, given the complex modalities of the services negotiations. In these negotiations commitments follow a positive list approach, there is no standard set of restrictions that can be monitored (such as tariffs in goods trade), and the restrictiveness of individual impediments to trade is difficult to gauge.

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[8] Only 30 WTO members have presented bilateral requests. Press reports suggest that, among developing countries, these include Chile, China, Hong Kong SAR, India, the Mercosur countries, Mexico, Panama, Pakistan, Peru, and Thailand.

[9] Proposal by Bolivia, Colombia, Cuba, Ecuador, Nicaragua, Peru, and Trinidad and Tobago. Other developing countries, notably African countries, have been less visible.

16. **There is significant tension between developing country aspirations and political constraints in the advanced countries with regard to Mode 4 supply of services** (the temporary movement of natural persons). This is an area whose economic potential, according to some estimates, could eclipse those of other topics under negotiation. India and other developing countries have targeted a range of restrictions in developed country markets related to economic needs tests, the processing of visa applications, residency requirements, recognition of educational qualifications, and social security contributions.

17. **The EU has submitted bilateral requests covering a variety of sectors, and the European Commission has developed a services offer for discussion by EU member states.** While envisaging market access commitments in a variety of sectors, it is understood that the offer seeks to protect the provision of public services within the EU, and emphasizes the right of the EU to design its own appropriate regulatory frameworks.[10] According to EU negotiators, the proposal accommodates requests made by developing countries on Mode 4 services.[11] Despite the improved offer from the EU, some developing country commentators complain that recognition of education requirements will be a major barrier to entry, unless mutual recognition agreements are signed across a wide range of professions or current recognition agreements are open to the accession of developing countries.

18. **The United States is seeking increased market access in 11 major service sectors and is requesting that countries remove nontransparent and discriminatory barriers to the commercial presence of U.S. firms.** The United States is also seeking increased access for temporary entry and stay for professional employees. The U.S. offer "locks in" liberalization that has taken place at the state and federal level since 1994.[12] Importantly, this could include developments such as the passage of federal legislation to modernize financial services, banking and insurance sectors. As regards horizontal commitments, notably for Mode 4 services, the U.S. offer deals mainly with salespersons and intra-corporate transferees.

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[10] The offer provides no commitments on audiovisual, education or health services.

[11] The proposal indicates that self-employed skilled professionals, working in certain sectors (e.g., computer services and engineers), and skilled employees of overseas companies with contracts to provide services with a client in the EU will be able to enter the EU for up to six months to provide services to EU clients. However, the Commission's proposal may be revised by the Member States.

[12] The U.S. offer does not provide foreign service companies with significant new market access. Some commentators point out that the United States already has one of the most open services markets in the world.

19. **WTO Members recently agreed on modalities for the treatment of (mostly unbound) autonomous liberalization measures taken unilaterally since the previous multilateral negotiations.** Liberalization has at times proceeded in the context of Fund programs, and developing countries have expressed concerns about a loss of negotiating leverage resulting from such liberalization. The modalities establish criteria for assessing the value of autonomous liberalization measures, as well as the principle that credit for such measures is to be advanced through bilateral negotiations. With regard to developing countries, it is emphasized that the modalities shall be used "as a means of promoting economic growth and development in developing countries and their increasing participation in trade in services."[13]

B. Negotiations on Trade Rules

Special and Differential Treatment

20. **For many developing countries, a successful outcome to the Doha Round requires obtaining significant concessions on SDT.** The Doha Declaration spelled out the hope of an "early harvest" of SDT and implementation issues by July 2002. However, two deadlines were missed, and the General Council has suspended formal discussions and encouraged members to conduct informal consultations.

21. **While there is a broad array of SDT and implementation proposals, in substance most seek either to exempt eligible countries from WTO disciplines (or soften them) or deal with capacity shortfalls in meeting such disciplines.** Many developing countries argue that WTO disciplines, for example, with regard to subsidies, trade-related investment measures or balance of payments safeguards, can unduly constrain development policies. Others contend that disciplines are, quite to the contrary, supportive of economic development by reducing uncertainty and limiting the scope for capture by vested interests. They point out that there is little evidence to suggest that—outside a narrow set of contexts—development interests are served by protection. There is broader agreement on the need to help countries develop the capacity to implement common rules, although there are differences over the establishment of a duty to provide such assistance. A further key point of contention is the criteria for eligibility—at present developing country status in the WTO is conferred through self-declaration.[14] As indicated in Table 2, prospects for compromise appear currently to be limited to certain agreement-specific proposals.

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[13] WTO Members are also discussing the development of modalities for the special treatment of LDCs. The development of these modalities is progressing smoothly, with LDCs particularly active.

[14] LDCs form a distinct group based on UN criteria.

Table 2. Summary of Negotiations on Trade Rules:
Negotiating Areas and Key Negotiating Positions

Antidumping (AD) measures

The negotiations are being driven by the "Friends of Antidumping Negotiations" Group, India, and the United States. The main elements of their contributions are as follows:

- The **"Friends"** consider that:

  (1) the AD rules are being abused as a protectionist tool;
  (2) there is a need for a clearer definition of the key concepts in the AD Agreement, improvements in the margin calculations, and greater transparency in AD investigations.

- The **United States**:

  (1) opposes most changes sought by the "Friends";
  (2) emphasizes the need to focus on procedural issues in AD investigations, their transparency, trade-distorting practices, and circumvention.

Non-agricultural subsidies

Cross-sectoral disciplines

The relatively few submissions to date propose expanding the category of prohibited subsidies, improving the serious prejudice provisions, and clarifying the rules in respect of tax-based subsidies, indirect subsidies, and natural resource pricing, as well as special and differential treatment for developing countries. In addition, some participants have suggested covering work on steel subsidies taking place at the OECD.

Fishery subsidies

The major players are the EU, Japan, Korea, and the informal group "Friends of Fish" (which includes the United States). The main elements of their positions are:

- **"Friends of Fish"** strongly advocate significant disciplines on fisheries subsidies.
- **Japan and Korea** strongly oppose sector-specific cuts in subsidies and contend that trade distortions caused by subsidies should be addressed as a cross-sectoral issue.
- **The EU** has indicated that it is moving increasingly in favor of reduced fisheries subsidies.

Table 2. Summary of Negotiations on Trade Rules:
Negotiating Areas and Key Negotiating Positions (continued)

Regional trade agreements (RTAs)

The negotiations focus on clarifying and strengthening rules on RTAs. Main contributors so far have included the EU and Australia.

- **EU** has emphasized that the negotiations should focus on clarification of existing WTO rules on RTAs and ways to improve their review in WTO bodies.
- **Australia** has advocated more fundamental reform of the rules governing RTAs. Specifically, it has sought a tightening of the rules on permissible derogation in RTAs from WTO commitments, ways of regulating existing RTAs multilaterally, and notification disciplines.

Special and differential treatment (SDT)

Strongly divisive debate between developing countries (led by India, Brazil, the African group, and other LDCs) and the developed countries.

- **Developing countries** have sought a considerable widening of SDT provisions and improving their precision and effectiveness, including changing the language in existing WTO agreements, to make SDT mandatory, rather than relying on "best endeavor" provisions.
- **Developed countries** are generally opposed to dealing with cross-cutting SDT issues through amending the text of WTO agreements, binding technical assistance commitments, or providing automatic derogations to WTO rules. However, they seem prepared to discuss the agreement-specific SDT proposals that have been advanced by developing countries in the relevant negotiating bodies.

TRIPS and public health

An area of great importance to many developing countries, particularly LDCs, this remains deadlocked because of differences between the U.S. position and that of developing countries.

- The **United States** insists that compulsory licensing (i.e., allowing the use of a patent without the consent of the patent-holder) and the right to import generics should apply only to a limited and specified set of diseases.

- **Developing countries**, in contrast, are insisting on an open-ended list of diseases.

22. **Another issue viewed as critical by developing countries is the public health clause of the TRIPS Agreement.** While the Doha Declaration confirms the authority of governments to suspend intellectual property rights on medicines in confronting threats to public health, there is disagreement over the circumstances under which a country may import generic drugs from third parties. A proposal that would have granted developing country authorities significant discretion in determining eligible public health emergencies has been blocked by the United States, which has called for a more narrow definition. In view of the emotionally charged debate over this issue, it is possible that this will be one of the principal challenges facing Ministers in Cancún. There is some concern that delays beyond Cancún could prove disruptive to the entire round.

Antidumping, Subsidies, and Regional Trade Agreements

23. **Efforts are being made by an informal group of countries (the "Friends of Antidumping Negotiations")[15] to meet the Doha mandate to clarify and improve disciplines in the WTO Antidumping Agreement** (see Table 2). The number of antidumping (AD) investigations has grown rapidly over the 1990s, and there is widespread concern over their use for protectionist purposes, as the WTO increasingly constrains recourse to more traditional forms of protection. The "Friends" contend that AD rules are being abused, accusing some countries of manipulation in calculating dumping margins, of arbitrary injury determination, and inaccurate causation analyses. Accordingly, the group advocates a clearer definition of the key concepts in the AD Agreement and improvements in the methodology for margin calculations, with a view to restricting discretion in antidumping investigations. The United States has taken a narrower focus in the debate—on transparency, procedures, and circumvention—and has not yet indicated a willingness to consider a more substantial agenda.

24. **The negotiations on non-agricultural subsidies have centered on cross-sectoral disciplines and fisheries subsidies, with the latter receiving most attention to date.** Recently the number of submissions addressing cross-sectoral subsidy issues has increased (Table 2). The push for sector-specific rules on fisheries subsidies is led by an informal group of developed and developing countries called the "Friends of Fish."[16] Essentially, the group is proposing a substantial cut in allowable fisheries subsidies of types which, in their view, lead to overexploitation of fishery resources and damage competition. On the other hand, Japan and Korea, in particular, insist on a cross-sectoral approach to subsidies and argue that the

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[15] This group includes Brazil, Chile, Colombia, Costa Rica, Hong Kong SAR, Israel, Japan, Korea, Mexico, Norway, Singapore, Switzerland, Taiwan Province of China, Thailand, and Turkey.

[16] Participants in this group include Argentina, Australia, Chile, Ecuador, Iceland, New Zealand, Norway, Peru, Philippines, and the United States.

case has not been made for the development of sector-specific subsidy disciplines in respect of fisheries. While it is broadly felt that freer and less distorted global trade requires improved disciplines on subsidies, it is too early to tell what approach might be taken, once the process moves into more active negotiation mode.

25. **No progress of substance has been achieved in the talks on regional trade agreements (RTAs).** The negotiations have so far focused on one issue—transparency. Some commentators suggest that this is disappointing, fearing that the proliferation of bilateral and regional agreements might undermine the multilateral system. They stress the importance of clearly defining the criteria according to which RTAs must cover "substantially all trade" in order to be permissible (Article XXIV of the GATT (1994)).[17] The possibility that existing RTAs might be grandfathered may further reduce the practical value of any multilateral agreement. There is a view that the limited ambition shown by members (developed and developing) in tightening disciplines on RTAs can be explained by their own, fairly extensive plans, to conclude further RTAs in the near future.

Singapore Issues

26. **The Doha Declaration envisages a decision "by explicit consensus" at the Cancún Ministerial on whether to pursue negotiations over the so-called Singapore issues**—an international investment framework, disciplines on competition policy, transparency in government procurement, and rules for trade facilitation. Working groups were set up to develop the modalities for such negotiations. The EU, their main proponent, argues that disciplines in these areas are a logical complement to the liberalization of border restrictions. Furthermore, an international framework for investment would be simpler, more transparent and more comprehensive than (proliferating) bilateral investment treaties (BIT). It would not restrict national policy autonomy any further than the BITs, if it were based on a GATS-style positive list approach (see also below in Section V). Nevertheless, a number of developing countries have argued that the WTO architecture, which relies on binding and actionable commitments, is inappropriate to deal with what they view fundamentally as problems of development. Others stress the costs of implementing agreements in these areas and are questioning their priority from a national development perspective. After sharp initial disagreements, the more recent debate has been less heated and some see common ground emerging, particularly on competition and trade facilitation.

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[17] Generally, it is required that RTAs cover "substantially all" trade between the members. Informally, some commentators interpret this to mean at least 80 percent of all trade but there is no formal definition of the concept.

III. Selected Issues of Relevance for the Fund

27. **A number of issues have arisen in the course of negotiations that intersect with aspects of the Fund's work.** As the remit of the WTO expands and deepens, particularly with regard to financial services and investment, its overlap with areas of Fund expertise is set to grow. Negotiating parties have emphasized the need for coherence with the activities and the mandate of the Fund and have requested Fund staff to contribute to the discussions.[18] The following section reviews aspects of discussions in four areas that call for close coordination in the period ahead. The intention is to flag the issues, not to attempt to resolve them nor to propose a particular course of action. Fund and WTO staff will work through the technical channels established in the WTO-IMF Cooperation Agreement to further clarify these issues, as the negotiations evolve.

A. Financial Services Liberalization and Financial Stability

28. **Discussions in the Committee on Trade in Financial Services have been broad in scope, and have included a number of areas of interest and relevance to the work of the IMF.** Most prominent among them are the impact of liberalizing financial services on the capital account; the pace and sequencing of financial liberalization; and the links between prudential regulation, transparency rules, and financial services liberalization.

29. **The overlap between financial services and capital account liberalization is not entirely a new issue for the WTO.** Many WTO members had limited their commitments on financial services in earlier GATS negotiations on the grounds that rapid liberalization might result in destabilizing capital flows.[19] Liberalization in the financial sector under the GATS was largely limited to binding of existing practices on the right of establishment and national treatment for foreign financial institutions, principally in the banking sector. Liberalization

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[18] Over the course of the past year Fund staff have been invited to give presentations on the Heavily Indebted Poor Country (HIPC) process and on the international financial architecture (Working Group on Trade, Debt and Finance); on the FSAP (Committee on Trade in Financial Services); and on managing the revenue implications of tariff liberalization (Like-Minded, LDC, and Africa Groups). Upon request by the WTO Director-General, Fund staff have prepared research notes on aspects of the SDT debate and on the revenue implications of tariff reform. The Fund/staff also contribute routinely to trade policy reviews, accession working parties, and the proceedings of the WTO Committee on Balance of Payments Restrictions.

[19] A recent Board seminar paper by the Fund's Research Department, "Effects of Financial Globalization on Developing Countries: Some Empirical Evidence" (SM/03/62, February 12, 2003), provides some support for these concerns, in particular in countries where liberalization evolves in a weak domestic policy and regulatory environment.

did not entail a more general elimination of restrictions on capital account transactions and did not constrain members in determining the appropriate pace and sequencing of capital account liberalization or in the use of capital account restrictions for macroeconomic or balance of payments reasons. In the past few months, a number of developing countries have again brought this issue to the fore and have indicated that clarification of the links between financial services and capital account liberalization would be a prerequisite to undertaking new and meaningful commitments in the GATS.

30. **The link between market access agreements on specific financial services and their potential impact on the capital account is not well understood by all members.**[20] In some cases, liberalization of trade in financial services can be synonymous with capital account liberalization.[21] Liberalizing the cross-border provision of deposit taking activities, for example, is equivalent to allowing residents to move capital abroad. In other cases, the impact on the capital account may be negligible, e.g., liberalizing the provision of financial advisory services. In still other cases, liberalization of a particular service activity may later give rise to gray areas, as financial innovation outstrips the host country's regulatory regime. For example, liberalization of market access for certain debt instruments could, as a side effect, result in the development of financial derivatives or trading activity based on these instruments outside the country of issue. As a result, there is uncertainty over the appropriate pace and sequencing of financial services liberalization, which may need to be addressed in the context of a careful assessment of individual circumstances.

31. **The prudential carve-out clause.** Article 2(a) of the Annex on Financial Services to the GATS allows for restrictions on trade in financial services, which members can impose unilaterally on prudential grounds to safeguard the integrity of their financial system. At present, there is no formal agreement in the GATS on what constitute prudential measures, and members are not obliged to notify the WTO of restrictions imposed under this clause. Furthermore, there are no articulated, detailed criteria for assessing whether actions taken under the prudential umbrella are "essential" for averting a potential threat to the financial system. This blanket carve-out reflects the relative youth of the GATS, compared to the GATT, which has been negotiated over several decades. There is general agreement,

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[20] This is, in fact, an area that has drawn little research in the past. Research, including by the Fund, has tended to focus on the interaction between domestic financial reforms and capital account liberalization. For instance, country experience suggests a number of general principles for the pace and sequencing of capital account liberalization. However, a similar body of knowledge on the sequencing of the liberalization of trade in financial services does not exist.

[21] This may be particularly the case under Modes 1 (cross-border supply) and 3 (commercial presence). The GATS distinguishes two further modes of service provision, namely consumption abroad, and the temporary movement of persons for the provision of services.

however, that the use of the prudential carve-out must be justified on some grounds, and greater clarity on the use of the carve-out would come through cases brought for dispute resolution or as the GATS evolves.

32. **Some WTO members are proposing to link liberalization to verifiable benchmarks and transparency rules.** Although this proposal has not been fully fleshed out in the Committee on Trade in Financial Services, a rules-based approach would presumably bind members in their commitments to the extent that a perceived violation would be actionable under WTO dispute settlement procedures. Such an approach may have its merits, but it also raises a number of questions regarding verification and the relation with voluntary sets of standards and codes, including those promoted by the Fund.[22]

33. **The Fund has been advising its members and evaluating performance in each of these areas—financial liberalization, prudential regulation, and adherence to standards.** In recent years, it has deepened its engagement in the assessment of financial sector performance and vulnerabilities under the Financial Sector Assessment Program (FSAP), undertaken jointly with the Bank. This offers scope for mutually beneficial cooperation, but also bears certain risks of overlap and the possibility of conflicting signals from two international institutions with a largely shared membership, and will need to be monitored closely. In particular, the binding nature of the WTO's rules-based approach might raise concerns over how the IMF can play its role in promoting transparency and stability in the financial sector without becoming entangled in the legal aspects of future disputes.

B. The International Investment Framework

34. **At Doha, ministers recognized the case for a multilateral investment agreement in the WTO, though negotiations will only start in earnest on the basis of explicit consensus at the Cancún Ministerial.** The ambition for the WTO investment agreement, as stated in the Doha declaration, is "to secure transparent, stable and predictable conditions" for international investment. This may be particularly important for small low income countries with weak institutions. Proponents argue that, as in other areas of international trade, the WTO could serve as a commitment device and help enhance investor confidence by emphasizing transparent regulations, while leaving members the flexibility to determine the extent of liberalization of investment conditions.[23] According to some proposals, the

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[22] While a full set of rules governing aspects of financial services activity would naturally be the product of multilateral negotiation, a preliminary analysis of proposals made thus far shows substantial similarity to the Fund's Code of Monetary and Financial Policy Transparency.

[23] Bilateral and regional trade and investment agreements already contain many of the elements that are sought for the WTO investment agreement, such as investor protection or national treatment for established investors. However, the proliferation of such treaties is (continued...)

agreement would also cover national treatment for potential investors. This would overcome the current disparity with investment in services sectors for which the GATS already provides certain disciplines for both pre- (i.e., market access) and post-establishment investment in the sectors included in members' schedules of commitments.

35. **For the time between the Doha and the Cancún ministerial meetings, the WTO working group on trade and investment has sought to clarify a number of technical aspects of a possible negotiating mandate.** As yet, no consensus for investment negotiations has emerged, and agreement may be subject to progress in the entire range of negotiations presented in Cancún. Aspects of the negotiations, especially in case of a broad definition of investment, may potentially intersect with the Fund's work and will be monitored closely by Fund staff as the mandate for WTO investment negotiations evolves.

36. **Investments covered by an eventual agreement.** The Doha Ministerial Declaration refers to "long-term cross border investment" as the object of the investment agreement. Accordingly, a number of WTO members have proposed a narrow definition of investment, most easily operationalized as foreign direct investment (FDI). However, others argue that the objective should be to protect established investors and encourage potential ones, and hence call for an "asset-based" investment definition.

37. **An asset-based investment definition would be in line with modern practice in bilateral and regional investment agreements, which protect the assets of foreign owned companies, independently of how these assets had been financed.** Its proponents draw a parallel with the GATS, in which WTO members have agreed to admitting those capital flows that are related to providing a service through commercial presence, should the sector in question be scheduled for this mode of supply. By contrast, a transactions-based approach (such as "cross-border" investment or FDI) would exclude finance other than from parent companies that the affiliates of multinational companies access both outside and within their host countries.

38. **As views on scope and definitions still diverge, WTO members have proposed a "hybrid" approach.** According to this approach, only a narrow set of investments would benefit from pre-establishment liberalization (i.e., the right to invest), and an asset-based approach would be applied to established investors. Clarifying the definition of investment in the WTO agreement may determine the agreement's success in establishing itself as a benchmark vis-à-vis the multitude of bilateral and regional investment agreements.

39. **A WTO investment agreement will also introduce new balance of payments safeguards.** This could help to address the concerns of developing countries in the WTO who fear that investment liberalization, especially if based on a broad definition of

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likely to raise the cost of doing business, and may discriminate among investors, thereby distorting international investment flows.

investment, could substantially restrict their ability to control certain flows in emergency situations and prevent them from safeguarding the stability of their balance of payments. In the negotiations, members will have to consider issues such as the definition of an event that gives rise to safeguards, the scope of their application to current and capital account transactions (both inflows and outflows), and the duration of safeguards.

40. **Apart from the Fund's general role and interest in advising members on balance of payments matters, a WTO investment agreement might also raise specific issues of interaction with the WTO.** One such issue is the Fund's potential responsibilities in the context of balance of payments safeguards, an issue raised by a number of countries in the WTO Working Group on Trade and Investment. In this regard, the GATS may provide a reference point. According to GATS Article XII, safeguards imposed at the member's initiative are narrowly circumscribed, and the member is required to consult in the WTO Committee on Balance of Payments Restrictions, which in turn will base its conclusions on the Fund's assessment of the member's balance of payments position. Another issue that may require clarification as negotiations progress is jurisdictional. The definition of investment under a WTO agreement could potentially overlap with aspects of current international transactions as defined in Art. XXX of the Fund's Articles of Agreement (e.g., "moderate amounts ... for depreciation of direct investment"), and it will be necessary to ensure that no uncertainties emerge over the Fund's jurisdiction.

C. The Revenue Implications of Trade Liberalization

41. **Many developing countries, particularly low-income countries and small economies, continue to rely heavily on trade taxes as a source of government revenue.** With the ongoing Doha Round, and the increasing number of regional integration schemes, concerns have emerged that further trade liberalization might be constrained by fears of revenue loss and fiscal deterioration. The issue has been raised in the ongoing discussions in a number of WTO bodies, where some developing countries have identified it as a serious impediment to further tariff concessions.

42. **Recent work by the IMF demonstrates that trade tax revenues have tended to decline in importance over the last decade, but still typically account for 15–25 percent of tax revenues in developing countries.**[24] For certain groups of countries the ratio can be significantly higher, e.g., the small island economies of the Caribbean where it averaged 40 percent in the period 1990–99.

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[24] IMF estimates indicate that trade tax revenue in Africa as a percentage of total revenue was approximately 30 percent in 1991–95 and just over 25 percent in 1996–99. See the recent note by the Fiscal Affairs Department, "Liberalizing Trade and Safeguarding Public Revenue," in the paper prepared for the WTO, "WTO Notes and Cover Letter from Ms. Krueger," (EB/CWTO/03/2, January 27, 2003).

43. **Nevertheless, potential revenue losses are empirically very small and three factors further mitigate the impact of tariff reductions on fiscal revenue:**[25]

- The ongoing Doha negotiations are based on bound rates, while revenue effects result from changes in applied rates. Therefore, if the changes in applied rates are more modest than the changes in bound rates, the revenue consequences may be less significant.

- To the extent that liberalization leads to the tariffication of quantitative restrictions and is accompanied by steps to rationalize the structure of tariffs, e.g. by reducing exemptions, it increases tariff revenue rather than reducing it.

- Average collected tariff rates by region, which often underlie empirical estimates of the revenue impact of further liberalization, may be misleading. Average collected rates obscure much variation, both across countries and products. For instance, reductions concentrated disproportionally in peak tariffs, as under some of the proposed formulas, might lead to an *increase* in revenue, if the current rates significantly constrain imports. More generally, tariff reductions can stimulate imports, which helps offset some revenue loss.

44. **Countries that do face a genuine problem may be able to balance the loss of trade taxes with revenue from other sources.** It is the overall tax revenue that is vital to the government's fiscal position. Experience and economic theory both suggest that indirect taxes—excises and a sales tax levied on a broad range of commodities (increasingly in the form of a value-added tax (VAT))—have a critical role to play.[26] In principle, it is possible to reduce dependence on trade taxes and switch to taxes on domestic consumption, while preserving the efficiency gains from the reduction in trade distortions. A switch that leaves consumers no worse off might actually cause government revenue to increase. Such an outcome can be achieved by combining tariff reductions with increases in domestic commodity taxes that entirely offset the impact on domestic prices. The benefits are clear:

- consumers are unaffected by the change in tax policy, as they face the same prices for the goods they buy;

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[25] Country experience also suggests that tariff reduction reduces tax evasion, in some cases significantly. See, for example, evidence on China in Raymond Fisman and Shang-Jin Wei, "Tax Rates and Tax Evasion: Evidence from 'Missing Trade' in China," NBER Working Paper No. 8551 (National Bureau of Economic Research: Cambridge, MA, 2001).

[26] A VAT—levied at each stage of production (so as to secure revenues) but with a crediting mechanism to avoid interfering with production decisions—is now in place in 130 countries, including some of the poorest.

- the prices producers face are closer to world market prices, better aligning private incentives with the country's comparative advantage; and
- the government now collects revenue at an unchanged total rate (tariffs plus commodity taxes combined) on a wider base, since domestic consumption (the base of the commodity tax) can be no less than imports (the base of the tariff).[27]

45. **Concerns about the practicality of such a strategy have been largely allayed by recent experience, often in the context of IMF technical assistance.** Even poorer developing countries have demonstrated their administrative ability to implement VAT schemes within relatively short periods of time, although experience underlines that sequencing issues need to be addressed, as well as the importance of continued administrative effort after their introduction.[28]

46. **Possible revenue losses associated with tariff reforms should therefore not be seen as an impediment to further trade liberalization.** Finance Ministries can facilitate progress under the Doha Round by pursuing tax reforms that reduce dependence on trade taxes. Fund staff was invited to elaborate on this message at a seminar directed at developing country negotiators in Geneva, and the Managing Director has expressed the Fund's readiness to the WTO to assist members, on a case-by-case basis, in identifying revenue trade-offs and in designing remedial action.

IV. Conclusions

47. **The slippages on the initial timeline for the Doha Development Agenda raise the pressure for results at the Cancún Ministerial meeting on September 10–14.** The agenda for Cancún is becoming increasingly complex, and success will require preparing the political ground for compromise, above all on agriculture, the public health provisions of the TRIPS agreement, and special and differential treatment for developing countries.

48. **In view of the wide gap in negotiating positions, progress in the Doha Round is unlikely to be made without determined and more courageous political leadership in the major trading powers, especially for agriculture.** For the development dimension of the round not to remain a rhetorical construct requires a readiness to step above the mercantilist exchange of concessions that has driven negotiations and to do so in areas, in which domestic

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[27] Conversely, if government decided to increase the commodity tax rate only to the level to which revenue is unchanged then consumer prices would ultimately fall (so consumers gain). The allocational efficiency gains of trade liberalization are secured and the fiscal position is no worse.

[28] See EB/CWTO/03/2, note on "Liberalizing ..." (see footnote 23 above).

political resistance has held back progress in the past. Success also requires a clear commitment to the spirit of the rules-based multilateral trading system and to less restrictive trade regimes on the part of the developing countries. An excessive focus on exceptionalism is neither good development policy, nor likely to advance the overall progress of the round.

49. **Open trade can be a powerful source of growth, and growth is the single most effective means of reducing poverty.** Perhaps unlike past rounds of multilateral trade negotiations, the Millennium Development Goals add urgency to achieving progress in Cancún—and beyond—without diluting ambitions. In a world of ever-growing capital flows, greater trade integration can also lessen vulnerabilities to financial crises. In these and other respects, the missions of the Fund and of the WTO are closely intertwined.

50. **The negotiations are showing up a number of areas in which the emerging responsibilities of the WTO and the interests of the Fund are likely to overlap, in particular in financial services and investment.** Within the coherence framework set out at Marrakesh the WTO Secretariat and Fund staff have developed a close and fruitful cooperation on these and other matters. In the period ahead, this framework can be built upon in order to delineate more clearly how both institutions can be mutually supportive, while acting within their mandates, and whether any additional institutional mechanisms might be called for in order to ensure coherence.

Annex Table 1. WTO Multilateral Trade Negotiations—Timeline

Deadline	**Issue Area**	
	Single undertaking negotiations on: implementation; agriculture; services; industrial tariffs; subsidies; antidumping; regional trade agreements, and environment.	**Negotiations on a separate track:** Dispute Settlement Understanding.
By June 30, 2002	**Services:** Members to submit initial requests for specific commitments.	
By July 31, 2002	**Textiles and clothing:** Council for Trade in Goods to report to the General Council and make recommendations on appropriate action regarding the methodology for calculating quota levels for small suppliers and accelerating quota growth. **Special and Differential Treatment:** Committee on Trade and Development to report to the General Council on making special and differential treatment provisions more efficient and/or mandatory (deadline missed and extended to December 31, 2002, when it was missed again). **Subsidies:** Committee on Subsidies and Countervailing Measures to report on its review of the SCM Agreement's provisions on countervailing duty investigations.	
By end-2002	**Intellectual property.** TRIPS Council to recommend solutions on effective use of compulsory licensing (deadline missed). **Antidumping.** Committee on Antidumping Practices to draw up recommendations on the application of antidumping measures to developing countries and the timeframe to be used in determining the volume of dumped exports. **Implementation issues.** Relevant WTO bodies to report to the Trade Negotiations Committee—for appropriate action—on their work on implementation issues for which the Ministerial Declaration does not provide a specific mandate (deadline missed).	
By March 31, 2003	**Agriculture.** Members to establish "modalities" for achieving objectives of the negotiations on agriculture (deadline missed). **Services.** Members to submit initial offers on specific commitments.	
By May 31, 2003	**Dispute Settlement Understanding.** Members to conclude negotiations. **Industrial goods.** Members to establish "modalities" for achieving objectives of the negotiations.	
September 10–14, 2003	**Fifth WTO Ministerial Conference.** WTO bodies to reports on full range of issues in the work program agreed in Doha. **Agriculture.** Members to submit comprehensive draft schedules. **New issues.** Members to decide by "explicit consensus" on modalities (including whether/when) for launching negotiations on investment, competition policy, transparency in government procurement, and trade facilitation. **Environment.** Committee on Trade and Environment to report to the Ministerial Conference on the need to clarify WTO rules—including the desirability of negotiations—with regard to the effect of environmental measures on market access; the relevant provisions of the TRIPS Agreement; and labeling requirements for environmental purposes.	
January 1, 2005	**Multilateral trade negotiations.** Members to conclude the negotiations under the single undertaking.	

Source: WTO Secretariat.

Annex Table 2. WTO Multilateral Trade Negotiations—Synopsis

Areas of negotiations	Issues under consideration	WTO body/Chairperson
	Market access negotiations	
Agricultural goods	• Tariffs, tariff quotas, trade preferences • Export subsidies and export credits • Domestic support and problems of classification • Food security and safety; special safeguards • Development box, food aid, rural development, environment	Committee on Agriculture, Special Session
Services	• Market access commitments in 12 services sectors • Liberalization of trade in financial services • Clarification, strengthening of rules • Treatment of autonomous liberalization	Services Council, Special Session
Industrial goods	• Tariffs and trade preferences • Capacity-building measures and technical assistance	Negotiating Group on Non-Agricultural Market Access
	Negotiations on WTO rules	
Antidumping measures	• "De minimis" dumping margins • Application of contracted values and the lesser duty rule • Application of the "cumulation" clause	Negotiating Group on Rules
Subsidies and countervailing measures	• "De minimis" level of permissible subsidies • Special treatment for export subsidies in developing countries • Rules for imposing countervailing duties on developing countries' exports • Fisheries subsidies disciplines • Export credits disciplines	
Regional trade agreements (RTAs)	• Thresholds for meeting RTA requirements under GATT • Extent of permissible derogation from WTO rules in RTAs • Relations between rules on RTAs in WTO agreements	
Trade-related intellectual property rights	• Establishment of a multilateral system of notification and registration of geographical indications for wines and spirits • Protection of geographical indications	Council for TRIPS, Special session
Environment	• Relationship between MEAs and WTO rules • Information exchange between MEAs and WTO • Market access in environmental goods and services • The definition of "environmental goods"	Committee on Trade and Environment, Special Session
Dispute settlement	• Rules on compensation and suspension of concessions • Number of Appellate Body members • System of permanent panelists	Dispute Settlement Body, Special Session
	Key horizontal issues	
Special and differential treatment for developing countries	• Identification of non-mandatory SDT provisions in WTO agreements to be made mandatory and their legal and practical implications • Ways of making SDT provisions more precise, effective, and operational	Committee on Trade and Development, Special Session
Implementation	• Special needs of LDCs and net food-importing countries • Extension of transition periods under TRIMs • Methodological issues in the fields of non-agricultural subsidies, customs valuation, and antidumping	All relevant WTO bodies