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WTO and SOEs: Overview of Article XVII and related
provisions of the GATT 1994

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Abstract

By acting as a trader, a State may influence the direction of international trade through its purchases and sales decisions without resort to other more direct means of intervention such as the application of tariffs and quotas. The GATT recognizes that States may choose to participate in international commerce in competition with private firms, but it does not leave them with a free hand when it comes to carrying out their trading activities. The core rules regulating a State's trading operations are found in Article XVII and related provisions of the GATT 1994. In the 70 years since their adoption, developments in both the GATT 1947 and the WTO have uncovered a set of seldom employed and relatively shallow disciplines rooted in the principle of non-discrimination, raising doubts about their relevance to the kinds "State trading" activities undertaken today. It remains true, however, that while State trading enterprises continue to operate across the world, and fundamental questions about the full reach and scope of the existing rules endure, it cannot be excluded that the limits of Article XVII and related provisions of the GATT 1994 may well be explored in the future practice of WTO Members, thereby clarifying their regulatory function in the modern trading system.

Keywords

STEs, SOEs, Article XVII, China

1. Introduction*

One of the fundamental objectives of the GATT is to liberalize international trade by reducing the degree of government interference in the trading decisions of private enterprise. Because it is generally presumed that governments, as opposed to private traders, will not always be motivated to achieve the most efficient allocation of resources, the GATT introduces a series of limits and disciplines on the ability of governments to influence trading markets, anticipating that this will improve aggregate economic welfare both within nations and across international boundaries.¹ The principal focus of these rules is the regulation of "traditional" trade policy instruments such as tariffs and quotas, internal taxation and the use of contingent trade protection. However, the GATT also addresses other less obvious ways in which a government may distort the movement of goods across borders, including through State trading.

By acting as a trader, a State may influence the direction of international trade through its purchase and sales decisions without resort to other more direct means of trade regulation. The GATT recognizes that States may choose to participate in international commerce in competition with private firms, but it does not leave them with a free hand in how to carry out their trading operations. Several provisions of the GATT specifically regulate the extent to which a State may participate in the market as a trader, with the core rules set out in Article XVII (State trading), Article II:4 (mark-ups applied by import monopolies) and the Interpretative Notes *Ad* Articles XI-XIV and XVIII (restrictions made effective through State trading operations).² This paper briefly outlines the origins of these provisions and provides an overview of how their main elements have thus far been interpreted and applied within the context of the GATT and the WTO.

2. Overview of the negotiating history

The origin of Article XVII and related provisions of the GATT 1994 can be traced back to the very genesis of the GATT in the United States' 1945 Proposals for the Expansion of World Trade and Employment.³ In this first set of proposals for how to shape the post-War international trading order, the United States promoted the idea that world trade could be expanded for the benefit of all participating nations by tackling what were then perceived to be four major problems: (i) restrictions imposed by governments; (ii) restrictions imposed by private combines or cartels; (iii) fear of disorder in the markets for certain primary commodities; and (iv) irregularity, and the fear of irregularity, in production and employment.⁴ The United States' proposals described a series of rules and principles

* A longer version of this paper was presented during the 2016 Columbia Law School Trade Seminar Series on State-Owned Enterprises in China: Trade and Competition Issues. Any views expressed are solely attributable to the author and not the WTO Secretariat.

¹ Jackson, J.H., Davey, W.J., Sykes, A.O., *Legal Problems of International Economic Relations: Cases, Materials and Text*, 6th Edition, 2013, pp. 22-30 and 228; Jackson, J.H., *World Trade and the Law of the GATT*, 1969, pp. 329-330.

² Articles XX(d) and XXXVII of the GATT also deal with State trading. Article XX(d) prescribes that nothing in the GATT shall prevent the adoption or enforcement by any Member of measures necessary to ensure compliance with laws or regulations relating to *inter alia* the enforcement of monopolies operated under Articles II:4 and XVII. Article XXXVII:3(a), which is part of Part IV of the GATT and deals with "Commitments", states that developed country Members shall make every effort, in cases where a government determines the resale price of products wholly or mainly produced in the territories of developing country Members, to maintain trade margins at equitable levels. Neither of these provisions is specifically examined in this paper.

³ Proposals for Expansion of World Trade and Employment, Developed by a Technical Staff within the Government of the United States in Preparation for an International Conference on Trade and Employment and Presented for Consideration by the Peoples of the World, U.S. Department of State, November 1945 ("United States 1945 Proposals").

⁴ United States 1945 Proposals, p. 2.

intended to serve as the starting point for multilateral discussions on how each of these issues might be addressed.⁵

Within the United States' proposals, the potentially distortive impact of State trading was perceived to be one of the species of governmental barriers to trade needing to be addressed. The main concern with State trading at the time was that purchases and sales decisions (of particularly State trading monopolies) could be taken in such a way as to cause serious obstacles to international trade by, for example, discriminating between countries, raising the resale price of imports or artificially restricting the amount of imported or exported products. State trading enterprises could, therefore, be potentially operated to undermine the trade benefits of disciplines limiting the use of other more transparent trade policy instruments such as tariffs and quotas.

The United States' initial proposals sought to address these concerns by coupling a general "equality of treatment" obligation calling for countries involved in State trading to ensure that their "foreign purchases and sales" are "influenced solely by commercial considerations", with two more specific obligations intended to secure a minimum level of market access from countries operating "monopolies of individual products" or "complete monopolies of foreign trade".⁶

A more elaborated version of these proposals was presented less than one year later in the United States Suggested Charter for an International Trade Organization.⁷ The United States' Suggested Charter became the main focus of the International Conference on Trade and Employment convened by the United Nations in February 1946,⁸ which within two years would produce both the GATT 1947 and the 1948 Havana Charter for an International Trade Organization.⁹ Not unlike the United States' 1945 Proposals, the Suggested Charter sought to regulate State trading by introducing a general rule of equality of treatment, this time presented as a principle of "non-discrimination" (Article 26), along with two provisions dealing with "State monopolies of individual products" (Article 27) and "complete State monopolies of import trade" (Article 28).

Article 26 of the Suggested Charter sought to ensure that the trading operations of covered enterprises approximated those of private traders by requiring that the purchases and sales activities of State trading enterprises ("STEs") be undertaken on a *non-discriminatory* basis, solely in accordance with *commercial considerations*. The United States explained that this obligation was intended to operate as "the counterpart of the most-favoured-nation clause as applied to ... customs duties".¹⁰ Under the terms of Article 27, countries operating import monopolies were called upon to *negotiate the mark-up* applied on domestic sales of the imported product. For the United States, this obligation would ensure that mark-ups were negotiated "in the same way as tariffs",¹¹ thereby safeguarding a minimum level of market access that might otherwise be undermined or not afforded at all were countries' import monopoly operations left unregulated. Finally, the United States explained that the rationale underlying Article 28, which required any country operating a "complete or substantially complete monopoly of its import trade" to *negotiate minimum purchase agreements*, was to

⁵ Letter from William L. Clayton, Assistant Secretary of State, to the United States Secretary of State, 1 November 1945, United States 1945 Proposals, p. IV.

⁶ United States 1945 Proposals, Section E, State Trading, p17.

⁷ Suggested Charter for an International Trade Organization of the United Nations, U.S. Department of State, September 1946 ("United States Suggested Charter").

⁸ Report of the First Session of the Preparatory Committee of the United Nations Conference on Trade and Employment, EPCT/33, p. 3.

⁹ For a succinct account of how the GATT developed in tandem with the Havana Charter for an International Trade Organization, see Jackson, Davey and Sykes, *ibid.*, pp. 230-233.

¹⁰ Preparatory Committee of the International Conference on Trade and Employment, Verbatim Report of the Fifth Meeting of Committee II, London, 30 October 1946, EPCT/CII/PV5, ("London Preparatory Committee, EPCT/CII/PV5") p. 36.

¹¹ London Preparatory Committee, EPCT/CII/PV5, pp. 36-37.

approximate the "general effect of reductions in duties and other trade barriers by countries whose trade is handled largely or mainly by private enterprise" – "in other words, ... allow imports to supply a larger share of the home market".¹²

The disciplines that are today applied to STEs through the operation of Article XVII and related provisions of the GATT 1994 reflect an effort to pursue the first two of these three objectives. The proposed rule that would have required countries operating complete or substantially completely monopolies of their import trade to undertake global purchase agreements was abandoned, having never been discussed in any substance by the GATT and Havana Charter negotiators.¹³ No replacement provision has ever been adopted.

3. Content and coverage of the main Disciplines

3.1 Non-discrimination

Using much the same language found in the United States' original proposals, the principle that State trading is to be undertaken on a non-discriminatory basis is given effect in the GATT 1994 through Article XVII:1, which is divided into three sub-paragraphs and reads as follows:

1.* (a) Each contracting party undertakes that if it establishes or maintains a State enterprise, wherever located, or grants to any enterprise, formally or in effect, exclusive or special privileges,* such enterprise shall, in its purchases or sales involving either imports or exports, act in a manner consistent with the general principles of non-discriminatory treatment prescribed in this Agreement for governmental measures affecting imports or exports by private traders.

(b) The provisions of subparagraph (a) of this paragraph shall be understood to require that such enterprises shall, having due regard to the other provisions of this Agreement, make any such purchases or sales solely in accordance with commercial considerations,* including price, quality, availability, marketability, transportation and other conditions of purchase or sale, and shall afford the enterprises of the other contracting parties adequate opportunity, in accordance with customary business practice, to compete for participation in such purchases or sales.

(c) No contracting party shall prevent any enterprise (whether or not an enterprise described in subparagraph (a) of this paragraph) under its jurisdiction from acting in accordance with the principles of subparagraphs (a) and (b) of this paragraph.

The language of these three sub-paragraphs gives rise to a number of legal and practical questions, including with respect to the following matters: (i) the types of *enterprises covered* by the disciplines; and (ii) the *substantive requirements* of the general principles of non-discrimination.

3.1.1 Covered enterprises

Three distinct types of entities are covered by the terms of Article XVII:1: (i) "a State enterprise, wherever located" that is established or maintained by a Member ("State enterprise"); (ii) "any enterprise" that is granted "formally or in effect, exclusive or special privileges" ("privileged enterprise"); and (iii) "any enterprise", whether or not a "State enterprise" or "privileged enterprise". Under the terms of sub-paragraphs (a) and (b) of Article XVII:1, Members undertake to ensure that the

¹² London Preparatory Committee, EPCT/CII/PV5, p. 37.

¹³ Second Session of the Preparatory Committee of the International Conference on Trade and Employment, Report to Commission A by Sub-Committee on Articles 31 and 32, 9 August 1947, EPCT/160, p. 8. It appears that one of the main reasons why this proposal was dropped is because the Soviet Union (at the time considered to be the only large trader that was likely to operate a complete monopoly of its import trade) did not participate in the meetings of the Preparatory Committee. See, Wilcox, C., *A Charter for World Trade*, The Macmillan Company, 1949, pp. 101-102; and Dam, K.W., *The GATT: Law and International Economic Organization*, Chicago University Press, 1970, p. 316.

operations of the first two types of enterprises are conducted in a manner consistent with the general principles of non-discrimination. Article XVII:1(c), on the other hand, imposes a negative obligation on Members *not to prevent* "any enterprise" from acting on a commercial basis. Whereas the nature of this third type of covered enterprise is self-explanatory, understanding what exactly amounts to a "State enterprise" or a "privileged enterprise" has proven to be more elusive.

Although "State enterprises" were initially defined as enterprises over whose operations a government exercises effective control,¹⁴ this definition was deleted from the final version of Article XVII, with drafters ultimately viewing the language of sub-paragraph (a) to describe the kinds of enterprises that should be covered by the disciplines "as precisely as is practicable".¹⁵ In fact, it was recognized early on in the negotiations that State trading activities were varied and not very well understood and, consequently, that it would be best to avoid being overly prescriptive in describing the coverage of the relevant disciplines.¹⁶ There is, therefore, no definition of the types of enterprises falling within the scope of Article XVII, with the only specific guidance left by the original drafters set out in one of its Interpretative Notes, which clarifies that "marketing boards" will be subject to the disciplines of Article XVII:1 only when they engage in *purchasing or selling* activities (thereby leaving *purely regulatory* "marketing boards" outside of the reach of Article XVII:1).¹⁷

The absence of a clear definition of State trading was raised a number of times during the history of the GATT 1947,¹⁸ but only directly addressed during the Uruguay Round,¹⁹ one of the key outcomes of which was the Understanding on the Interpretation of Article XVII. The Understanding introduced the following "working definition" of STEs:

Governmental or non-governmental enterprises, including marketing boards, which have been granted exclusive or special rights or privileges, including statutory or constitutional powers, in the exercise of which they influence through their purchases or sales the level or direction of imports or exports.²⁰

The "working definition" is explicitly stated to be without prejudice to the substantive provisions of Article XVII. A number of observations can be made about its content. First, it limits STEs to enterprises granted "exclusive or special rights or privileges". Commentators have argued that this is narrower than what is provided for under Article XVII because it excludes State enterprises that are not granted "exclusive or special privileges" from its scope of operation, a limitation that is not found in text of Article XVII:1(a).²¹ Second, the "working definition" confirms that "privileged enterprises" may include entities afforded the power to make purchases or sales by operation of *national legislation or constitutional prerogatives*. However, it does not otherwise explain what is meant by "exclusive or special rights or privileges". Third, the "working definition" envisages that covered enterprises will be those that "influence" international trade "through their purchases or sales", saying

¹⁴ Report of the Drafting Committee of the Preparatory Committee of the United Nations Conference on International Trade and Employment, New York, 5 March 1947, EPCT/34, p. 28.

¹⁵ EPCT/160, Note 12, p. 6.

¹⁶ See, e.g., EPCT/CII.36, p. 11 (United States); ECPT/A/PV.15 pp. 15-23 (various); and EPCT/CII/37, pp. 1-4 (various).

¹⁷ Interpretative Notes *Ad* Article XVII:1.

¹⁸ See, e.g., discussion in Notifications of State-Trading Enterprises, Final Report adopted on 24 May 1960, 9th Supp. BISD 179 ("1960 Notifications Panel Report"), p. 180

¹⁹ See, e.g., Article XVII (State Trading Enterprises), Note by the Secretariat, Negotiating Group on GATT Articles, MTN.GNG/NG7/W/15, 11 August 1987, paras. 13-17.

²⁰ Understanding on the Interpretation of Article XVII, para. 1.

²¹ See, e.g., Petersmann, E-U, GATT Law on State Trading Enterprises: Critical Evaluation of Article XVII and Proposals for Reform, pp. 71-96 at pp86-87, in Cottier, T. and Mavroidis, P. (eds), *State Trading in the Twenty-First Century*, University of Michigan Press, 1998.

nothing about whether any specific degree of "influence" would suffice for this purpose.²² Nevertheless, by requiring that such influence result from "*purchases or sales*" activities, the "working definition" does reveal that the *nature* of the operations of a particular enterprise will be an important factor to consider when determining whether it falls within the scope of Article XVII. Moreover, the "working definition" does not explicitly tie the "purchases or sales" activities to *imports or exports*, suggesting that an enterprise need not actually import or export itself in order to be covered by Article XVII.²³

Another important result of the Uruguay Round was the establishment of the Working Party on State Trading Enterprises, which was tasked with *inter alia* developing an illustrative list of the kinds of relationships between governments and STEs, and the kinds of activities engaged in by such enterprises, for the purpose of Article XVII.²⁴

The Working Party's Illustrative List was produced in 1999 on the basis of information contained in STE notifications since 1980, and is intended to provide non-binding guidance only.²⁵ It explains that a "notifiable state trading enterprise" has two essential features: (i) first, it must have "a relationship to government through the latter's granting of a right or privilege"; and (ii) second, it must conduct "an activity which influences the level or direction of imports and exports".²⁶ In terms of *relationships between notifiable entities and government*, a broad spectrum of different associations are presented, ranging from entities that are branches of government, government-owned or partially government-owned, to entities that are entirely separate from the government but established and maintained under legislation and financed and controlled by the producers of the product over which they may have marketing authority.²⁷ As regards the types of *activities engaged in by notifiable enterprises*, the Illustrative List sets out a non-exhaustive list of at least 17 operations considered to be of a kind "which *might* be engaged in by a state trading enterprise", emphasizing that "*no one activity or combination of activities necessarily identifies an enterprise as falling within the agreed WTO definitions of 'state trading enterprise'*".²⁸ It is apparent from the broad, non-exhaustive and non-binding nature of the guidance set out in the Illustrative List that Members have continued to shy away from developing a comprehensive definition of STEs, preferring the flexibility that comes with the existing broadly-worded text of Article XVII and the "working definition" – an observation that is arguably supported by the fact that the definitional issue has never been raised in GATT or WTO dispute settlement.

3.1.2 Substantive requirements

3.1.2.1 Most-favoured-nation and national treatment obligations?

One of the recurring questions concerning the interpretation of Article XVII:1 is whether the obligation to conduct purchases or sales operations involving either imports or exports "in a manner consistent with the general principles of non-discriminatory treatment in the {GATT} for governmental measures affecting imports or exports by private traders" extends beyond a requirement

²² According to Davey, this omission represents a possible element of vagueness in the definition. Davey, W., *Article XVII GATT: An Overview*, p. 25 in Cottier, T. and Mavroidis, P. (eds), *State Trading in the Twenty-First Century*, University of Michigan Press, 1998.

²³ The same clarification was made in the 1960 Notifications Panel Report.

²⁴ Understanding on the Interpretation of Article XVII, para. 5.

²⁵ Illustrative List, para. 2.

²⁶ Illustrative List, para. 6.

²⁷ Illustrative List, para. 8.

²⁸ Illustrative List, para. 9 (emphasis added).

of *most-favoured-nation treatment* and includes a *national treatment* obligation.²⁹ While the national treatment rule specified in Article III would obviously catch any action on the part of an STE taking the form of the types of governmental measures falling within its scope of operation (namely, taxes and other internal charges, laws, regulations and requirements affecting the internal marketing and sale of imported products), an STE's "*purchases or sales*" operations may not always be covered.³⁰

The negotiating history suggests that the principle of non-discrimination that is enshrined in Article XVII:1 was not intended to include a national treatment obligation. In the United States' original proposal, the notion of non-discrimination was described in terms of "non-discriminatory treatment" "compared with the treatment accorded to the commerce of any country other than that in which the enterprise is located".³¹ A subsequent draft of the negotiating text was even clearer in this regard, specifying that the "commerce of other Members shall be accorded treatment no less favourable than that accorded to the commerce of any country, other than that in which the enterprise is located".³²

1.1. This understanding of the negotiating history is reflected in the report of the GATT Panel in the 1952 *Belgian Family Allowances* case, where the panel found that the non-discrimination obligation in Article XVII:1 "did not extend to matters dealt with in Article III".³³ However, in subsequent disputes,³⁴ GATT Panels have taken a more cautious approach, never fully entering into the merits of claims grounded in the existence of a national treatment obligation in Article XVII after making findings of inconsistency of the challenged measures with other provisions of the GATT. Nevertheless, in the *obiter dictum* of one of these disputes, the 1984 *Canada – FIRA* case, the GATT Panel "saw great force in Canada's argument that only the most-favoured-nation and not the national treatment obligations fall within the scope of the general principles referred to in Article XVII:1(a)."³⁵

In order to clarify the situation, the United States submitted a proposal during the Uruguay Round calling for an explicit recognition that "the national treatment obligation or Article III applies to state trading".³⁶ However, there was little appetite among the participants to negotiate such substantive matters. Nevertheless, soon after the establishment of the WTO, the question was once again brought before a panel in the *Korea – Various Measures on Beef* dispute. In this proceeding, Australia challenged certain beef tendering practices of a Korean STE, which Australia claimed *inter alia* afforded less favourable treatment to imported beef compared to domestic beef in violation of Article XVII:1.³⁷ Not unlike the GATT-era panels, the WTO panel in *Korea – Various Measures on Beef* chose not to make any specific finding on the merits of Australia's Article XVII:1 (national treatment)

²⁹ See, e.g., Davey, pp. 17-33.

³⁰ Cf. Roessler, who argues that the "national treatment provisions of Articles III:2 and III:4 ... are sufficiently broadly worded to capture the denial of national treatment to imported products through state trading operations". Roessler, F., *Comment: Canada – Wheat: discrimination, non-commercial considerations, and the right to regulate through state trading enterprises*, (2008) 7 World Trade Review 1, pp. 67-69 at p. 69.

³¹ United States Suggested Charter, Article 26.

³² First Session of the Preparatory Committee held in London in 1946. London Report, First Session of the Preparatory Committee, EPCT/33 ("London Report"), p. 32.

³³ GATT Panel Report, *Belgian Family Allowances*, G/32, adopted 7 November 1952, BISD 1S/59 at p. 60 para. 4.

³⁴ GATT Panel Report, *Canada – Administration of the Foreign Investment Review Act*, L/5504, adopted on 7 February 1984, BISD 30S/140 ("*Canada – FIRA*"); GATT Panel Report, *Canada – Import, Distribution and Sale of Alcoholic Drinks by Canadian Provincial Marketing Agencies*, L/6304, adopted on 22 March 1988, BISD 35S/37; and GATT Panel Report, *Canada – Import, Distribution and Sale of Alcoholic Drinks by Canadian Provincial Marketing Agencies*, adopted on 18 February 1992, DS17/R, BISD 39S/27.

³⁵ GATT Panel Report, *Canada – FIRA*, p. 163, para. 5.16.

³⁶ State Trading: Proposal by the United States, MTN.GNG/NG7/W/55, 13 October 1989, at p. 2.

³⁷ Panel Report, *Korea – Various Measures on Beef*, para. 770.

claim, ruling instead in favour of Australia with respect to the same measures on the basis of claims made under Articles II and XI of the GATT.³⁸

Thus, despite having multiple opportunities to rule upon complaints premised on the view that Article XVII:1 imposes a *national treatment* obligation on the purchases or sales operations of STEs, both GATT-era and WTO panels have avoided making any findings on the question, saying very little, if anything, about the matter. Because complaints have always been pursued in relation to STE measures or conduct impugned under other GATT provisions, it has to date never been necessary for a panel to fully explore and resolve an Article XVII:1 national treatment claim. While this means that the Article XVII:1 national treatment question remains unsettled, any gap in the disciplines applicable to STEs that might be caused by this uncertainty has, thus far, not adversely affected the interests of complaining Members, given that the practices challenged under Article XVII:1 in all of the relevant disputes were, ultimately, found to be inconsistent with other GATT provisions.

3.1.2.2 Do sub-paragraphs (a) and (b) of Article XVII impose distinct obligations?

Article XVII:1(b) clarifies that the obligation in Article XVII:1(a) to make purchases or sales involving imports or exports in a manner consistent with the principle of non-discrimination "shall be understood to require" STEs to "make any such purchases or sales solely in accordance with commercial considerations" and "afford the enterprises of other contracting parties adequate opportunity, in accordance with customary business practices, to compete for such purchases or sales". The relationship between these two sub-paragraphs and, in particular, the extent to which they prescribe *distinct legal obligations* was one of the main questions that arose in the *Canada – Wheat Board* case, the only WTO dispute to have thus far resulted in *both* panel and Appellate Body findings with respect to the operation of Article XVII.

In this dispute, the United States challenged the export operations of the Canadian Wheat Board ("CWB"), arguing that they failed to respect the standards of non-discrimination set out in Article XVII:1 because they involved the use of the CWB's exclusive and special privileges to shut out competitors from making sales in particular export markets.³⁹ In advancing this line of argument, the United States submitted that sub-paragraphs (a) and (b) of Article XVII:1 imposed three *distinct* legal obligations on STEs: (i) to act in a manner consistent with the principles of non-discrimination (sub-paragraph (a)); (ii) to make purchases or sales solely in accordance with commercial considerations (sub-paragraph (b), first clause); and (iii) to afford the enterprises of all Members adequate opportunity to compete for participation in CWB's sales (sub-paragraph (b), second clause).⁴⁰

The panel did not take a position on the merits of the United States' legal interpretation, rejecting the United States' claim on other grounds.⁴¹ However, on appeal, the Appellate Body examined the United States' arguments more closely, finding that they could not be sustained. According to the Appellate Body, it was "abundantly clear" from the language of sub-paragraph (b) that the entirety of sub-paragraph (b) is "dependent upon the content of subparagraph (a)", and operates to clarify the scope of the requirement not to discriminate in subparagraph (a).⁴² Thus, while ruling out the possibility that a violation of Article XVII:1 could be established *solely* on the basis of a failure to satisfy one of the two requirements set out in Article XVII:1(b), the Appellate Body also effectively ruled that sub-

³⁸ Panel Report, *Korea – Various Measures on Beef*, para. 780.

³⁹ Panel Report, *Canada – Measures Relating to Exports of Wheat and Treatment of Imported Grain*, ("Canada – Wheat Exports"), paras. 4.182-4.188.

⁴⁰ Panel Report, *Canada – Wheat Exports*, para. 6.52.

⁴¹ Panel Report, *Canada – Wheat Exports*, paras. 6.58-6.59.

⁴² Appellate Body Report, *Canada – Wheat Exports*, para. 89.

paragraph (b) will become relevant only when the governmental action at issue is of a kind that should be governed by the principles of non-discrimination prescribed in sub-paragraph (a).⁴³

3.1.2.3 The meaning of "commercial considerations"

The requirement in Article XVII:1(b) that STEs must make their "purchases or sales solely in accordance with commercial considerations, including price, quality, availability, marketability, transportation and other conditions or purchase or sale" is clarified in two Interpretative Notes, the first of which reads as follows:

The charging by a state enterprise of different prices for its sales of a product in different markets is not precluded by the provisions of this Article, provided that such different prices are charged for commercial reasons, to meet conditions of supply and demand in export markets.⁴⁴

In exploring the United States' Article XVII:1 claims in *Canada – Wheat Exports*, the panel found that the clarification set out in this Interpretative Note implies that an export STE would not be acting inconsistently with the non-discrimination obligation in Article XVII:1(a), if it were to charge different prices for sales of the same products in different export markets, *provided that those prices were charged for commercial reasons*.⁴⁵ However, the United States' claims against the CWB's export operations were based on a different understanding of the obligation to act in accordance with "commercial considerations". In particular, the United States argued that the obligation to act solely in accordance with "commercial considerations" means that an STE's trading activities must be conducted in the same way as a commercial actor – that is, an economic entity that maximizes profits, does not enjoy government-conferred privileges or exclusive rights, and is disciplined by market forces.⁴⁶

The panel found nothing in the text of Article XVII:1(b) to support the United States' position. For the panel, the requirement that STEs act solely in accordance with commercial considerations simply means that they should seek to purchase or sell on the basis of "considerations pertaining to commerce and trade, or considerations which involve regarding purchases or sales 'as mere matters of business'".⁴⁷ Accordingly, the panel rejected the United States' argument that the first clause of sub-paragraph (b) should be interpreted so as to prohibit an export STE from using its exclusive or special privileges to gain a competitive advantage over competing "commercial actors", finding that the only constraint imposed on the use of exclusive or special privileges is that they be used to make sales which are driven exclusively by "commercial considerations".⁴⁸

The panel's findings were upheld on appeal, with the Appellate Body adding that it saw no basis for interpreting the disciplines in Article XVII, which are aimed at preventing certain types of discrimination, "as imposing comprehensive competition-law-type obligations on STEs".⁴⁹ According to the Appellate Body, the requirement to act solely in accordance with "commercial considerations" does not require STEs to refrain from using their privileges and advantages simply because such use might "disadvantage" private enterprises. STEs are entitled to exploit the advantages they may enjoy

⁴³ A similar view is expressed in GATT Panel Report, *Canada – FIRA*, para. 5.16.

⁴⁴ The second Interpretative Note that is relevant to the notion of "commercial considerations" is the specific Interpretative Note *Ad Article XVII:1(b)*, which provides that a "country receiving a 'tied loan' is free to take this loan into account as a 'commercial consideration' when purchasing requirements abroad". According to Jackson, this Interpretative Note was introduced in response to Chinese concerns that many countries in need of loans would not be able to obtain them in the absence of an exception to the "commercial considerations" requirement. Jackson, pp. 347-348.

⁴⁵ Panel Report, *Canada – Wheat Exports*, paras. 6.48-6.49.

⁴⁶ Panel Report, *Canada – Wheat Exports*, paras. 6.74-6.76 and 6.90-6.91.

⁴⁷ Panel Report, *Canada – Wheat Exports*, paras. 6.86-6.87.

⁴⁸ Panel Report, *Canada – Wheat Exports*, para. 6.103.

⁴⁹ Appellate Body Report, *Canada – Wheat Exports*, para. 145.

to their economic benefit, just like private enterprises.⁵⁰ Thus, the Appellate Body "saw force" in the panel's rejection of the United States "purposive interpretation", which attributed a very broad scope to Article XVII:1 without accounting for the disciplines on the operations of STEs found in other covered agreements, such as the SCM Agreement, Article VI of the GATT, the Anti-dumping Agreement and the Agreement on Agriculture.⁵¹

3.1.2.4 Affording an adequate opportunity to compete in purchases or sales

The second clause of Article XVII:1(b) requires that STEs afford the "enterprises" of other Members "adequate opportunity, in accordance with customary business practice, to compete for participation in {their} purchases or sales".

In *Canada – Wheat Exports*, the United States argued that this requirement imposed an obligation on the CWB to ensure that, in its export sales, any enterprise wanting to compete for participation as a potential wheat-buyer or as a wheat-selling producer, should be afforded an adequate opportunity to compete for those sales.⁵² The United States submissions were rejected by both the panel⁵³ and on appeal, with the Appellate Body ultimately explaining that the requirement to afford an adequate opportunity to compete for participation in such sales refers to the opportunity to become the STE's counterpart in the sales transaction itself, *not* to an opportunity to replace the STE as a participant in the transaction.⁵⁴

3.2 Preservation of negotiated market access concessions

Rules governing certain aspects of the operation of import monopolies are set out in Article II:4 GATT, which provides as follows:

4. If any contracting party establishes, maintains or authorizes, formally or in effect, a monopoly of the importation of any product described in the appropriate Schedule annexed to this Agreement, such monopoly shall not, except as provided for in that Schedule or as otherwise agreed between the parties which initially negotiated the concession, operate so as to afford protection on the average in excess of the amount of protection provided for in that Schedule. The provisions of this paragraph shall not limit the use by contracting parties of any form of assistance to domestic producers permitted by other provisions of this Agreement.*

Although there is no reference to "State trading enterprises" in Article II:4, it is generally recognized that this provision imposes disciplines on the mark-up practices of one particular kind of STE – an import monopoly. The basic rationale for the introduction of rules to moderate the pricing practices of import monopolies is that, left to their own devices, monopoly operators could potentially circumvent negotiated concessions by applying mark-ups on imported products sold on the domestic market at levels that would price them above domestically produced competing products. It would, therefore, be relatively easy for a monopoly importer to undermine the anticipated benefits of market access commitments by trading in a way that directly or indirectly resulted in raising the price of imported products to prohibitive or non-competitive levels.

Article II:4 endeavours to prevent this potential form of circumvention by requiring Members maintaining or authorizing an import monopoly to ensure that it is not operated so as to afford greater protection to a particular product than provided for in that Member's Schedule of concessions or as otherwise agreed between the parties that negotiated the concessions. Thus, absent a special agreement

⁵⁰ Appellate Body Report, *Canada – Wheat Exports*, para. 149.

⁵¹ Appellate Body Report, *Canada – Wheat Exports*, para. 150.

⁵² Panel Report, *Canada – Wheat Exports*, para. 6.61.

⁵³ Panel Report, *Canada – Wheat Exports*, para. 6.69.

⁵⁴ Appellate Body Report, *Canada – Wheat Exports*, para. 157 (emphasis original, footnote omitted).

between negotiating parties, the tariff bindings inscribed into a Member's Schedule of concessions will serve to define the level of protection that may be afforded to domestic producers through an import monopoly. In this respect, Article II:4 specifically provides that the degree of protection cannot "on average" exceed "the amount of protection provided for" in the relevant Member's Schedule.

Article II:4 is yet to be explored in WTO dispute settlement practice. However, it has been interpreted and applied in a number of GATT cases, which have laid down guidance for how to calculate the maximum prices and mark-ups that an import monopoly will be entitled to charge.

In terms of prices, the panel in *Canada – Provincial Liquor Boards (EEC)* found that an import monopoly must charge a price that does not exceed the landed cost of the imported product *plus* customs duties, transportation, distribution and other expenses incidental to its purchase, sale or further processing, as well as a reasonable margin of profit and any internal taxes.⁵⁵ The same panel also found that *differential* mark-ups on the internal sale of imported and domestic products could be levied by an import monopoly, provided that they reflect specific costs associated with the purchase or sale of the domestic or imported products.⁵⁶ Likewise, the panel in *Canada – Provincial Liquor Boards (US)* reached essentially the same conclusion, explaining that a *differential* mark-up should allow for the recovery of: (i) costs directly associated with the handling of the imported product; (ii) charges for fixed assets in proportion to the use of those assets by the imported product; and (iii) all other general and administrative expenses allocated uniformly to all domestic and imported products.⁵⁷ Finally, when it comes to profit margins, the panel in *Canada – Provincial Liquor Boards (EEC)* considered that monopoly importers are not entitled to earn monopoly profit, as this "could not normally be considered as a 'reasonable margin of profit' in the sense of Article II:4, especially if it were higher on imported products than domestic products."⁵⁸

3.3 Import and export restrictions made effective through STEs

Articles XI, XII, XIII, XIV and XVIII of the GATT set out the main rules applicable to the maintenance of quantitative import and export restrictions. A general prohibition on the application of quantitative restrictions is prescribed in Article XI:1, with Articles XII, XIII, XIV and XVIII describing when and the extent to which this obligation may be derogated from for balance of payments and economic development reasons. The Interpretative Note to these provisions reads:

Throughout Articles XI, XII, XIII, XIV and XVIII, the terms "import restrictions" or "export restrictions" include restrictions made effective through State trading operations.

The GATT, thus, recognizes that quantitative restrictions may be effected through not only direct government action, but also the purchases or sales activities of STEs. The most obvious way that an STE might be operated with this effect would be if an import monopoly were directed to make no or only limited purchases of imports. Such a factual scenario arose in *Japan – Agricultural Products*, where import restrictions imposed by a Japanese STE on certain agricultural products were found to be inconsistent with Article XI:1 on the basis of the Interpretative Note.⁵⁹

The same Interpretative Note has also been relied upon to successfully challenge the *distribution activities* of STEs possessing both monopoly import *and* distribution privileges. In *Canada – Provincial Liquor Boards (EEC)*, the distribution practices of the Canadian STEs which discriminated between imported and domestic products (by, e.g., limiting the points of sale of imported products

⁵⁵ GATT Panel Report, *Canada – Provincial Liquor Boards (EEC)*, p. 86, para. 4.10.

⁵⁶ GATT Panel Report, *Canada – Provincial Liquor Boards (EEC)*, p. 87, para. 4.13.

⁵⁷ GATT Panel Report, *Canada – Provincial Liquor Boards (US)* p. 81, para. 5.19.

⁵⁸ GATT Panel Report, *Canada – Provincial Liquor Boards (EEC)*, p. 87, paras. 4.15-4.16.

⁵⁹ GATT Panel Report, *Japan – Restrictions on Imports of Certain Agricultural Products*, L/6253, adopted 2 March 1988, BISD 35S/163 ("*Japan – Agricultural Products*"), p. 229, para. 5.2.2.2.

relative to domestic products) were found to be inconsistent with Article XI:1 because, in the light of the existing monopoly over imports *and distribution*, they effectively operated as restrictions on imports, within the meaning of the Interpretative Note.⁶⁰ Essentially the same line of reasoning was relied upon by the WTO panel in *Korea – Various Measures on Beef*, where the *distribution practices* of a Korean STE exercising exclusive importation and distribution rights over 30% of Korea's beef imports were found to amount to restrictions on beef *imports* inconsistent with Article XI:1.⁶¹

3.4 The 1954-55 GATT Review Session

The rules and disciplines on State trading contained in the original GATT 1947 were narrower in both scope and ambition compared to those set out in the Havana Charter of 1948. However, after it became apparent that the Havana Charter would not enter into force, the GATT contracting parties during the 1954-1955 GATT Review Session explored the possibility of amending the GATT 1947 to capture what had already been agreed and incorporated into the Havana Charter. It was decided that two new paragraphs would be inserted to: (i) create a role for mutually advantageous negotiations to address the adverse trade effects of State trading enterprises which might not be regulated by other existing disciplines; and (ii) introduce certain transparency requirements.⁶²

3.4.1 Negotiations to limit or remove obstacles to trade

Article XVII:3 provides that:

The contracting parties recognize that enterprises of the kind described in paragraph 1(a) of this Article might be operated so as to create serious obstacles to trade; thus negotiations on a reciprocal and mutually advantageous basis designed to limit or reduce such obstacles are of importance to international trade.*

Article XVII:3 envisages that negotiations may be undertaken with a view to limiting or reducing the obstacles created by STEs in the same way as tariff negotiations are used to secure market access.⁶³ The Interpretative Note to this paragraph clarifies that such negotiations "may be directed towards the reduction of duties and other charges on imports or exports, or towards the conclusion of any other mutually satisfactory arrangement" consistent with the GATT. To the extent that it encourages Members to enter into negotiations with a view to addressing the potential adverse trade effects of STE operations on negotiated market access concessions, Article XVII:3 broadly reflects the second of the three main objectives pursued by the United States' original proposals⁶⁴ which had evolved into Article 31:1 and 31:2 of the Havana Charter.

However, in practice, arrangements of the kind envisaged under Article XVII:3 appear to have most often been negotiated in the context of the accession to the GATT/WTO of countries considered to have non-market economies.⁶⁵ Thus, for example, minimum import purchase commitments were negotiated in the accession protocols of Poland (1967) and Romania (1971), with GATT Contracting Parties furthermore preserving a right to maintain their own import quotas on Polish and Romanian

⁶⁰ GATT Panel Report, *Canada – Provincial Liquor Boards (EEC)*, para. 4.24.

⁶¹ Panel Report, *Korea – Beef*, para. 766.

⁶² Reports Relating to the Review of the Agreement, *Other Barriers to Trade*, adopted 3 March 1955, BISD 3S/222 at 228 ("1955 Working Party Report").

⁶³ 1955 Working Party Report, at 228.

⁶⁴ See above, p. 2.

⁶⁵ See, in general, Davey, pp. 32-34.

exports.⁶⁶ The latter arrangement was also agreed with Hungary when it acceded to the GATT in 1974.⁶⁷

A somewhat broader range of commitments affecting the operations of STEs have been negotiated with more recently acceding Members of the WTO. Thus, for example, on joining the WTO, China undertook obligations in relation to *trading rights* and the liberalization of *State trading monopolies* in a number of sectors. In particular, China agreed to progressively liberalize the availability and scope of the right to trade, so that, within three years after accession all enterprises in China would have the right to trade in all goods, with the exception of those identified in one of the annexes to its Accession Protocol, which could continue to remain subject to State trading.⁶⁸ China accepted that it would phase out import quotas and import licensing requirements with respect to 377 products, some of which were traded through State trading enterprises.⁶⁹ Moreover, China agreed to progressively abolish State trading in respect of silk;⁷⁰ that imports allocated to non-State traders of crude and processed oil would be carried over to the next year if they were not fully utilized;⁷¹ and that it would ensure that no price increase imposed by State trading enterprises would result in protection beyond that allowed in its Schedule of Concessions.⁷² China also confirmed that it would ensure that all *State-owned* and *State-invested enterprises* would make purchases and sales based solely on commercial considerations, and that the enterprises of other WTO Members would have an adequate opportunity to compete for sales to and purchases from these enterprises on non-discriminatory terms and conditions. In addition, China undertook not to influence, directly or indirectly, commercial decisions on the part of State-owned or State-invested enterprises, including on the quantity, value or country of origin of any goods purchased or sold.⁷³

3.5 Transparency

With little known about the nature and full extent of State trading at the time of the GATT/ITO negotiations,⁷⁴ it was apparent that provisions would be needed to ensure adequate disclosure of information about the operations of STEs in order to secure the proper functioning of the adopted disciplines. Paragraph 4 to Article XVII was introduced for this purpose, partly reflecting Article 31:3 and 31:4 of the Havana Charter.⁷⁵

Article XVII:4 has four sub-paragraphs. Sub-paragraphs (a) and (c) require Members to notify the *products* that are the subject of an STE's import or export operations, and to furnish "*information*

⁶⁶ Protocol for the Accession of Poland, BISD 15S/46 at 52; and Protocol for the Accession of Romania, BISD 18S/5-10.

⁶⁷ Protocol for the Accession of Hungary, BISD 20S/3-8.

⁶⁸ Protocol on the Accession of the People's Republic of China, WT/L/432, ("China Accession Protocol") p4. China's *trading rights commitments* were the subject of a WTO dispute brought by the United States in 2007 with respect to certain Chinese measures concerning *inter alia* films for theatrical release and unfinished audiovisual products. The Chinese measures were found to be inconsistent with China's obligations. See, Panel Report, *China – Measures Affecting Trading Rights and Distribution Services for Certain Publications and Audiovisual Entertainment Products*, WT/DS363/R and Corr.1, adopted 19 January 2010, as modified by Appellate Body Report WT/DS363/AB/R, DSR 2010:II, p. 261.

⁶⁹ China Accession Protocol, p. 5 and Annex 3A pp. 43-60.

⁷⁰ Report of the Working Party on the Accession of China, 1 October 2001, WT/ACC/CHN/49 ("China Working Party Report"), para. 215.

⁷¹ China Working Party Report, para. 212.

⁷² China Working Party Report, para. 217.

⁷³ China Working Party Report, para. 46.

⁷⁴ See, generally, discussion in Jackson, pp. 333-334.

⁷⁵ Compare Article XVII:4(b) with Article 31.3 Havana Charter; and Interpretative Note *Ad* Article XVII:4(b) with Articles 31:3 and 31:4 Havana Charter.

about its operations" if considered by another Member to be adversely effecting its trading interests. Together, these provisions establish the legal basis for the core transparency and notification requirements in relation to STEs. The opportunity for Members to make "counter-notifications" where it is felt that another Member's notification is incomplete, incorrect or where no notification has been made, was introduced in the Understanding on the Interpretation of Article XVII.⁷⁶

3.6 Conclusion

Article XVII and related provisions of the GATT were originally introduced in an effort to ensure that the activities of STEs were conducted on terms and conditions approximating those of private traders and without negating the market access benefits achieved through the operation of other GATT disciplines. As State trading was a relatively new and unknown realm of international trade, drafters considered that agreement on a general set of rules and principles aimed at achieving this goal would suffice, anticipating that the negotiated outcomes would be fine-tuned and modified as necessary through their implementation.

In the 70 years since their adoption, developments in both the GATT 1947 and the WTO have delineated a set of seldom used and relatively limited disciplines rooted in the principle of non-discrimination. When considered in the light of the fact that the GATT was never expected to comprehensively regulate the activities of STEs in a way that would eliminate all of the potential obstacles to international trade they might cause,⁷⁷ this is not a surprising outcome. Indeed, the fact that a *separate and additional* set of disciplines on the "business practices affecting international trade" of "public commercial enterprises" was included in the Havana Charter,⁷⁸ would appear to confirm that Article XVII and related provisions of the GATT were not intended to regulate all manifestations of a State's participation as a trader in international commerce.

With the last formal dispute settlement complaint brought against an STE over 14 years ago,⁷⁹ and the continued resort to the inclusion of "WTO-plus" commitments in the protocols of accession of new WTO Members, doubts may well be raised about whether Members perceive the existing GATT disciplines as an effective tool to address the types of "State trading" activities undertaken today. The fact remains, however, that while STEs continue to operate across the world, and fundamental questions about the full reach and scope of the existing rules endure, it cannot be excluded that the limits of Articles XVII and related provisions of the GATT may be explored in the future practice of WTO Members, thereby clarifying their regulatory function in the modern trading system.

⁷⁶ Understanding on the Interpretation of Article XVII, para. 4. Thus far, only one counter-notification has been reviewed in the Working Party – the United States' August 2014 counter-notification of State trading enterprises allegedly operating in China. Counter-Notification of the State Trading Enterprises of China Pursuant to Paragraph 4 of the Understanding on the Interpretation of Article XVII, G/C/W/701-G/STR/Q1/CHN/2, 14 August 2014.

⁷⁷ See above, pp 8 and 11.

⁷⁸ Chapter V, Restrictive Business Practices, Havana Charter. Article 54 defines "public commercial enterprises" as "agencies of government insofar as they are engaged in trade" and "trading enterprises mainly or wholly owned by public authority".

⁷⁹ The United States requested consultations with the government of Canada in the *Canada – Wheat Exports* dispute on 17 December 2002, WT/DS276/1.

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