CONSULTATION UNDER ARTICLE XXII

Consultation with the Member States of the European Economic Community on Tobacco

DRAFT AGREED MINUTE

1. The consultation on tobacco under Article XXII of the General Agreement with the Member States of the European Economic Community which was held at the request of the Government of the Federation of Rhodesia and Nyasaland and which opened in Geneva on 23 October and 4 and 17 November 1958 was resumed in Geneva on 17, 19 and 25 February 1959. This minute relates to the February consultation only.

2. In addition to the Member States of the EEC the following other contracting parties participated in the consultation: Brazil, Canada, Cuba, Dominican Republic, India, Indonesia, Federation of Rhodesia and Nyasaland, Turkey and the United States of America. The Chair was taken alternately by a representative of participating countries other than the Six and by a representative of the Six. The representatives of all third countries took part in the discussions and in general the view of one representative was shared by others. For the sake of brevity, however, these views are recorded below not as the views of particular countries supported by others but as the views of "representatives of participating countries other than the Six". At their request, however, formal statements by the representatives of the Federation of Rhodesia and Nyasaland and of the United States have been attached as Annexes II and III, and memoranda submitted by the Governments of Turkey and the United States have been attached as Annexes IV and V.

3. The discussion was carried out in the light of data and discussion to be found in Add.6 to document L/805, the statistics furnished by the GATT secretariat (attached as Annex I), the discussions which had taken place in the previous consultation under Article XXII, and various memoranda

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1 With reference to the status of the United States, see paragraph 4 of the report on bananas (document Spec(59)66) and its annexed declaration by the Six.
(i.e., memoranda submitted by the Governments of the Federation of Rhodesia and Nyasaland, Turkey and the United States, and the reply of the Six which will be supplied as soon as possible and will be annexed to this document).

COMMON EXTERNAL TARIFF

(a) Implementation of the Common Tariff

4. The representatives of the Six stated in reply to questions about the present level of duties on tobacco that the position so far as France and Italy were concerned remained unaltered, i.e., State monopolies would continue to operate as before and no duty had yet been imposed; in the case of the Federal Republic of Germany and Benelux the position was:

(a) Federal Republic of Germany

Unmanufactured Tobacco - The duty of DM.180 per 100 net kgs. remained unaltered for third countries as the decision of 3 December 1958 taken by Member States of the EE badly took not apply to agricultural products, imports of which have been liberalized, and such is the case of tobacco in the Federal Republic of Germany; the duty, however, had been reduced on 1 January 1959 by 10 per cent to DM.162 per 100 net kgs. for EEC countries and the AOT's. No consumer tax was applied.

Cigarettes - The rate of duty for cigarettes which had been negotiated under GATT with the United States in 1956 remained unaltered at DM.7,500 per 100 net kgs. both for Members of the Community and for other countries.

(b) Benelux

Unmanufactured Tobacco - The rate of duty applied to Members of the Community and the AOT's had been reduced by 10 per cent on 1 January 1959 to Fl.28.71 per 100 net kgs. in the Netherlands and to B.frw.371.30 per 100 net kgs. in the BIEU. The 10 per cent reduction had not been applied to third countries.

Cigarettes - The rate of duty applied to third countries remained unaltered at 45 per cent but had been reduced by 10 per cent to 40.5 per cent for EEC countries and the AOT's.
(b) Assessment of the Common Tariff

5. In discussion on the assessment of the common tariff, representatives of participating countries other than the Six expressed the opinion that the rate of 30 per cent ad valorem for unmanufactured tobacco which had been agreed upon by the Six was unduly high considering that in France and Italy, where imports were made solely by State monopolies, there had been no tariff on tobacco on 1 January 1957, and in Benelux the duty had been relatively low, i.e., representing an ad valorem incidence of about 8 per cent on 1956 prices. In France and Italy the common tariff would represent an incidence much greater than 30 per cent since these countries proposed to maintain their tobacco monopolies.

6. These representatives recalled that during the previous consultation the spokesman for the Six had stated that the protection afforded by the monopolies was "total, complete or absolute" and that if a tariff equivalent were to be sought it would have to amount to at least 50 per cent ad valorem (Annex I to MGT(59)3(b)). They asked why, if the monopolies in France and Italy were to continue to exist, it had been thought necessary to take the protection afforded by these monopolies into account in establishing the common tariff. In their opinion double protection was afforded by the continued existence of State monopolies in France and Italy together with the overall introduction of a common tariff calculated by reference to these monopolies. There could be only two reasons for the increase of a tariff rate as an act of policy - either to increase revenue or to alter the pattern of trade for protective or other reasons. Since there had been no suggestion that the Six required additional customs revenue from tobacco it could only be assumed that the proposed discriminatory tariff was intended to change the pattern of tobacco imports into the EEC. If the monopoly system were to be extended to the whole common market this would further increase the incidence of the common tariff in the Federal Republic and the Benelux countries. Thus, the effective tariff for the common market would bear no relation to the previous tariffs of the Six.

7. The representatives of the Six recalled their statement during the first consultation, when they had pointed out that the rate of duty had not been fixed by computing the arithmetical average or weighted average of the legal duties or those actually applied, but had been negotiated between the Member States; it would have been very difficult from the technical point of view to apply either of those methods, since in France and Italy protection was not afforded
by means of the tariff, but through State monopolies. The representatives of certain third countries had asserted that additional protection was afforded by the juxtaposition of tariff protection on monopolies; in that connexion, the representatives of the Six tried to explain why there could be no question of additional protection, since by virtue of the existence of the monopolies, the protection afforded was already at a maximum level and could not be increased. The representative of the Six stated that the Member States had not yet turned their attention to the problem of adapting the monopolies to the new situation created by the Rome Treaty, and that for the time being no changes were therefore envisaged. He added that France continued to require foreign tobacco, and that the import programmes, which were not at all rigid, depended inter alia on market conditions, prevailing prices, and the qualities available.

8. The representatives of participating countries other than the Six noted that no final decision had yet been taken on the level of the common tariff on cigarettes because Member States might wish to notify the Common Market Commission in accordance with Article 17:2 of the Treaty of Rome that they considered that a fiscal element was included in the duties applied on 1 January 1957. They expressed the view that this fiscal element should be excluded in the calculation of the common tariff on tobacco as provided for in Article XXII of the General Agreement. 7

9. The representatives of the Six, while recognizing that negotiations under Article XXIV:6 of the General Agreement would have to be held where rates of duty which had previously been the subject of tariff concessions under GATT were involved, nevertheless reminded the other participating countries that although it had been agreed that such negotiations with regard to the common tariff should take place before it came into effect, there had been no suggestion that they need take place before the first modifications were made in the individual tariffs of the various Member States.

DEVELOPMENTS IN PRODUCTION

10. The representatives of participating countries other than the Six noted that since 1 January 1959 tobacco producers in the AOT's had had access to the German and Benelux markets at a rate of duty 10 per cent below that applied to
producers in third countries. They considered that the introduction of a 30 per cent margin of preference was bound to act as an incentive to greatly increased new investment and overall production in the overseas territories and was likely to result in a substantial diversion of trade from third countries. They stated that reports had already been received and official statements made that producers in these territories were planning to expand production. While other producing countries recognized that there was likely to be an expansion of production in the AOT's, they objected to this expansion being encouraged by the introduction of a 30 per cent margin of preference. They recalled the views on possible increases in production in the overseas territories which had been expressed in the report of the Working Party on the Association of the Overseas Territories with the European Economic Community (L/805/Add.6) and said that nothing had developed which altered these views.

11. The representatives of the Six stated that while it was possible that tobacco production, like that of other commodities, both in the AOT's and within the Community would increase as a result of economic development such development appeared to be limited by many factors which had been outlined in the answer which the Six had given to the memoranda submitted by third countries. Available statistics for production in the French overseas territories indicated that production was of relatively minor importance and that there had been no overall increase in recent years. In the countries of the Community, it was possible that Italian production would increase but competition from other expanding crops and the lack of available land for cultivation would no doubt tend to keep increases in the quantities produced within moderate limits. They further stated that the increases in consumption which it had been estimated would occur during the next few years, partly as a result of increased standards of living within the Community and overseas, would more than offset normal expansion of production within the area.
POTENTIAL DAMAGE TO NON-SIX PRODUCERS

(a) **Diversion of Trade**

12. In the view of participating countries other than the Six, the introduction of a discriminatory common tariff of 30 per cent on unmanufactured tobacco would, because of the effect on prices and of the stimulus to production which it would provide in the associated overseas territories, result in the gradual loss to producers in third countries of their markets within the Community. It was noted that such diversion was especially to be expected in Benelux and Germany where the new preferential effects would be the greatest. This diversion of trade would also cause damage to the trade in manufactured tobacco products where it was necessary for manufacturers to plan their blends well in advance, as the types of tobacco which they required might suddenly cease to be available to them at competitive prices. In this connexion, producing countries pointed out that the arrangements proposed concerning manufacture and sale of cigarettes by the French tobacco monopoly might lead to still further special advantage for French ACT producers at the expense of other suppliers. Specifically, it was noted that the French monopoly can and does manufacture and distribute cigarettes made to its own specification with tobaccos of its own choosing in Benelux while Benelux manufacturers have no comparable privilege in France. Hence, as tobaccos used heavily by the French monopoly began to enjoy tariff advantage in Benelux one could expect raw tobacco imports for the account of the monopoly to displace other tobaccos which Benelux countries might otherwise continue to buy from overseas sources. Similar non-reciprocal arrangements giving the French monopoly special advantages in manufacture and sale of cigarettes in other countries of the Community might also be established. Participating countries other than the Six shared the hope that the implementation of the EEC would result in a general increase in income and consumption in the area. It was nevertheless feared that because of the creation of a preferential barrier to trade third countries would not be permitted to share any increase in demand. Furthermore, if a substantial increase in demand was expected within the area, it was all the more difficult to understand why increased tariff protection and preferential treatment of the overseas territories was considered necessary. With respect to the consumption increases that the Six had forecast, the producing countries considered these to be higher than the levels likely to be attained especially as no per capita increase was to be expected in the Netherlands where there had been relatively free trade in tobacco.
13. The representative of the Six replied that the assumption made by the representatives of the countries which feared a diversion of trade was based on a number of special premises, such as a considerable increase in production in the ACT’s, stagnation in consumption, change in consumer taste, etc. etc., but he himself found great difficulty in believing that those premises would prove correct. What was known of the conditions of tobacco production in the overseas countries did not make it very likely that any really substantial increase in production would occur in coming years; as to consumption, authoritative studies had been made which showed, on the contrary, that it would rise by 75,000 tons by 1965, so that more would have to be bought from foreign suppliers. Furthermore, those studies had been made without making special allowance for the improvement in standards of living which should ensue when the Treaty came into force, and it was not unreasonable to believe that the prosperity thus expected would produce tangible effects.

(b) Substitution

14. Representatives of participating countries other than the Six stated that in the case of tobacco there was danger of substitution as manufacturers within the Community would turn more and more towards the type of tobacco produced within the preferential area, and, as consumer demand tended to be affected by price, the wide price difference permitted by a 30 per cent margin of preference would reflect heavily on all types of tobacco but more immediately on the more expensive types, and would thus cause a decrease in demand for tobacco imported from third countries. There was also, in their opinion, the additional possibility that production of the more expensive types of tobacco - cigar-wrapper, oriental, Burley, Maryland and flue-cured - would expand within the preferential area and thus replace even the amounts of such tobacco which might have continued to be imported from third countries for blending purposes.

15. The representative of the Six pointed out in reply that substitution trends were, in general, slowly evolving processes in which prices were not necessarily the decisive factor, as was proved by the example of the changes noted during the last war cited a year previously by third countries. It was well known that, especially with tobacco, which was not an article of necessity and, although widely consumed, still fell into the category of what might be termed the "superfluous", consumption on the whole was hardly affected by changes in price. Although the 30 per cent duty would obviously fall most heavily on the more expensive tobaccos, the Six doubted whether consumption
could be seriously affected, especially if allowance was made for the broad prospects of a rise in standards of living, which was the basic assumption of the Treaty.

16. The representatives of the Six also stated that, according to authoritative estimates, the consumption of tobacco in the EEC countries and in the AOT's would increase by 75,000 tons by 1965, which implied increased imports.

ASSessment Of Damage

17. No agreement was reached during the Consultation on the question of how damage to third countries could be assessed at this stage. Representatives of the Six stated that there was no proof that other producers were suffering actual damage already, and while they recognized that third countries had apprehensions about the future position, they did not believe that they would prove to have been justified. Without concrete evidence they could not accept the argument of the other participating countries that import and production trends within the Community and the associated overseas territories were already changing and that a serious threat to their trade was imminent.

18. The participating countries other than the Six urged the representatives of the Six to reconsider their decision regarding mitigation of damage. In their view damage to the trade of third countries would inevitably result from the proposed arrangements of the Six. They pointed out that they could not afford to wait until concrete evidence of damage became available (e.g. in statistical form) because by that time consumer tastes would have been altered and it would be very difficult to prevent lasting damage to the producers. It was added that the amount of duty borne by imports at a 30 per cent ad valorem rate would be progressively heavier by comparison with the tariff burden represented by a continuation of present specific tariffs since costs and prices of tobacco were likely to rise.

Conclusions

(a) Views of the Non-Six

19. Representatives of participating countries other than the Six stated that they were greatly concerned about the effects which the imposition of a discriminatory 30 per cent tariff would have from now on upon trade in tobacco which was of great importance to their economies. In their opinion the imposition
of a 30 per cent tariff calculated by reference to the French and Italian monopolies, which would, however, continue to operate, would constitute a substantial barrier to exports, particularly in the case of the Benelux countries and the Federal Republic of Germany, and would stimulate production in the AOT's; would lead to manufacturers in the metropolitan territories of the Six substituting types of tobacco grown in the AOT's for the various types of imported tobacco, with a resulting substantial diversion of the trade of the third countries. Since the Six anticipated a substantial increase in demand in the territories of the Six and the AOT's, the reasons for such a high level of discriminatory tariff protection were hard to understand. They urged the representatives of the Six to reconsider their decision to impose such a high tariff and to consider whether it should not be replaced by non-discriminatory internal taxes. They further expressed their apprehensions about the possible application of Articles 39 to 46 of the Treaty of Rome which might involve the use of long-term contracts and minimum prices, either of which could place third country products at a further disadvantage.

20. They expressed their disappointment that they must report to their Governments that no progress had been made during the consultations and that there was no sign of any practical action being taken by the Six to mitigate the effects of the damage to their tobacco exports which they felt must result. It was also disappointing in their opinion that the representatives of the Six had not been able to agree, despite the arguments which had been presented to them, that there was cause for concern about the future amongst other producing countries.

(b) Views of the Six

21. The representatives of the Six expressed their conviction that future prospects were far from being as gloomy as the other participating countries seemed to fear. Thus the incidence of the tariffs applied by the Federal Republic of Germany would be reduced from 32 per cent to 30 per cent and the adaptation of the French and Italian monopolies in accordance with the provisions of the Treaty of Rome would improve the position of non-Six producers. It was true that the Benelux tariff would be raised and that it was not expected that there would be any substantial rise in consumption per capita in Benelux during the next few years, but increases in population and in standards of living would bring about an appreciable rise in total consumption and this in turn would lead to increased tobacco imports.
22. While recognizing that the other participating countries experienced apprehension about future damage to their trade as a result of the Treaty of Rome the representatives of the Six observed that any discussion on the future was necessarily subject to considerable uncertainty and that, in any case, the fact that discussion had centred on possible future damage clearly showed that no actual damage was being suffered by third countries. They undertook to report the views expressed by other participating countries to the competent authorities and, on the request of the Federation of Rhodesia and Nyasaland, the United States and Turkey, to reply in writing to the memoranda submitted by those countries.