This paper, which reviews the operation of the GATT Balance-of-Payments Committee, has been prepared in response to a request made by the Working Group on Financial Services including Insurance at its July meeting (MTN.GNS/FIN/2). The paper contains the following sections:

(A) Articles XII (Restrictions to Safeguard the Balance of Payments) and XVIII:B (Government Assistance to Economic Development);
(B) Article XIV (Exceptions to the Rule of Non-Discrimination); and
(C) Article XV (Exchange Arrangements).

The information contained in this paper summarizes information previously presented in documents before the Negotiating Group on GATT Articles (MTN.GNG/NG7/W/14 and MTN.GNG/NG7/W/46), which may be referred to for further details on some of the issues under discussion.

The provisions of GATT Articles XII and XVII:B are currently under review in the Negotiating Group on GATT Articles. A summary of the current status of this review is contained in the report by the Chairman of that Group to the Group of Negotiations on Goods (MTN.GNG/NG7/W/73).
A. **Articles XII (Restrictions to Safeguard the Balance of Payments) and XVIII:B (Government Assistance to Economic Development)**

I. **History**

1. Articles XII and XVIII:B were put into their present form in October 1957, following an overall review of the General Agreement undertaken in 1955. Articles XII and XVIII:B have been amplified by detailed consultation procedures last codified in 1970 (BISD 18S), by "simplified" consultation procedures for developing countries introduced in 1972 (BISD 20S) and by provisions on the application of the Articles and consultation procedures laid down in the 1979 Declaration on Trade Measures Taken for Balance-of-Payments Purposes (BISD 26S/205), which extend the GATT examination of the balance-of-payments provisions from quantitative restrictions alone to all trade measures taken for balance-of-payments purposes.

2. Since 1979, few developed countries have invoked or maintained restrictions under Article XII, and none are currently doing so. Article XVIII:B is currently invoked by eighteen developing countries.

II. **Basic Provisions**

3. **Article XII** of the General Agreement provides contracting parties with a permitted deviation from the provisions of Article XI (General Elimination of Quantitative Restrictions) concerning the prohibition of quantitative restrictions on trade in goods. The aim of Article XII is to distinguish temporary measures taken for balance-of-payments purposes from quantitative restrictions applied for protective reasons, and to discourage the use of the former for the latter purpose. It lays down criteria for the level of restrictions to be applied (paragraph 2(a)). The Article also specifies that restrictions shall be progressively relaxed "as such conditions improve", that restrictions shall be maintained "only to the extent that" the reserves situation still justifies their application, and that restrictions shall be eliminated "when conditions would no longer justify their institution or maintenance" (paragraph 2(b)). It also establishes an essential link between trade measures for balance-of-

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1. i.e. that import restrictions instituted, maintained or intensified by a contracting party shall not exceed those necessary:

   (i) to forestall the imminent threat of, or to stop, a serious decline in its monetary services, or

   (ii) in the case of a contracting party with very low monetary reserves, to achieve a reasonable rate of increase in its reserves.
payments reasons and domestic adjustment policies (paragraph 3(a)), and lays down conditions permitting priority to be given to imports of products which are more essential and relating to the effects of measures on the commercial or economic interests of other contracting parties, "unreasonable" prevention of imports in "minimum commercial quantities", import of commercial samples and compliance with intellectual property procedures.

4. Article XVIII:B was drawn up in order to enable developing countries "to apply quantitative restrictions for balance of payments purposes in a manner which takes full account of the continued high level of demand for imports likely to be generated by their programmes of economic development" (Article XVIII, paragraph 2). It recognizes that developing contracting parties "tend, when they are in rapid process of development, to experience balance-of-payments difficulties arising mainly from efforts to expand their internal markets as well as from the instability in their terms of trade" (paragraph 8). The criteria for introducing balance-of-payments restrictions (paragraph 9) are similar to those of Article XII, but contain some differences of nuance and hence of wording. A developing country may control "the general level" of imports by restricting the quantity or value of imported goods. The purpose of such restrictions is "to safeguard its external financial position and to ensure a level of reserves adequate for the implementation of its programme of economic development". The appropriate level of such restrictions, specified in paragraph 9(a) and (b) is related to a "serious" decline in monetary reserves or, in the case of a contracting party with "inadequate" monetary reserves, a reasonable rate of increase in its reserves. In paragraph 9(a), the word "imminent", in relation to a threat of a serious decline in reserves, was not felt appropriate because "the reserve problem for these countries is one of the adequacy of the reserves in relation to their programme of economic development".

5. Article XVIII:B contains similar provisions to those of Article XII in respect of the relationship with domestic policies and the progressive relaxation of restrictions (paragraph 11). Like Article XII, the Article contains provisions permitting priority to be given to imports of products which are more essential in the light of a country's policy of economic development and provisions relating to effects on others' commercial or

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2 However, this is modified by recognition in paragraph 3(d) that domestic policies aimed at full employment may give rise to a high level of demand for imports and that contracting parties should not be required to withdraw or modify restrictions "on the ground that a change in these policies would render unnecessary restrictions which it is applying under this Article".

3 The questions of the "serious decline" "very low level" or "reasonable rate of increase" in monetary reserves are determined by the IMF under GATT Article XV, paragraph 2. (See paragraph [34] below)
economic interests, minimum commercial quantities, samples, and the observance of intellectual property provisions.

III. Schedules of Consultations

6. All restrictive import measures taken for balance-of-payments purposes are subject to examination under Article XII or Article XVIII:B, i.e. to consultation in the Balance-of-Payments Committee.

7. Paragraph 4 of Article XII, paragraph 4 sets out the basic provisions for annual consultations by developed countries applying balance-of-payments restrictions. Such consultations cover the nature of balance-of-payments difficulties, alternative corrective measures which may be available, the possible effect of the restrictions on the economies of other contracting parties, and any special external factors adversely affecting the export trade of the contracting party applying restrictions. Similar provisions are laid down in Article XVIII, paragraph 12(a) and (b) for consultations with developing countries, which are to be held 'at intervals of approximately, but not less than, two years'.

IV. The 1979 Declaration

8. The scope of balance-of-payments consultations was expanded from quantitative restrictions alone to "all" import-restrictive measures taken for balance-of-payments purposes in the 1979 Declaration on Trade Measures Taken for Balance-of-Payments Purposes (BISD 26S/205), which was adopted by the CONTRACTING PARTIES at the end of the Tokyo Round. The declaration also clarifies provisions relating to notification, consultation procedures, and the membership of the Committee on Balance-of-Payments Restrictions.

9. In drawing up the Declaration, the CONTRACTING PARTIES established a certain number of general principles which had not been previously spelled out, or which required amplification:

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4. The extension of balance-of-payments consultations to "all" measures resulted from the use of generalized import surcharges or deposit schemes by a number of countries in the 1960s and 1970s for balance-of-payments purposes. Such measures were not strictly justifiable under the letter of Articles XII or XVIII:B, but had nevertheless been defended as being less disruptive to trade than the quantitative restrictions which Articles XII and XVIII:B envisaged.

5. The Uruguay Round Negotiating Group on GATT Articles has received proposals suggesting draft texts of a new Declaration on Trade Measures taken for balance-of-payments purposes. See Chairman's Report to the GNG (MTN.GNG/NG7/W/73, July 1990, Annex 2)
(a) That restrictive trade measures "are in general an inefficient means to maintain or restore balance-of-payments equilibrium";

(b) That restrictive import measures taken for balance-of-payments purposes "should not be taken for the purpose of protecting a particular industry or sector" and that contracting parties should "endeavour to avoid that [such measures] stimulate new investments that would not be economically viable in the absence of the measures";

(c) That the less-developed contracting parties "must take into account their individual development, financial and trade situation" when implementing such measures, and that the impact of trade measures taken by developed countries on the economies of developing countries can be serious;

(d) That developed contracting parties "should avoid the imposition of restrictive trade measures for balance-of-payments purposes to the maximum extent possible".

10. Any "introduction or intensification" of measures taken for balance-of-payments purposes is to be promptly notified to the GATT. Reverse notifications may be made by any contracting party which has reason to believe that a restrictive import measure applied by another contracting party is taken for balance-of-payments reasons. The GATT secretariat may also be asked to seek information on a measure and make it available to contracting parties. (Paragraph 36 of NG7/W/14 lists the cases of recourse to these provisions in recent years.) Consultations shall be held "immediately after instituting or intensifying such restrictions (or, in circumstances in which prior consultation is practicable, before doing so)".

11. The 1979 Declaration introduced three new conditions for application of balance-of-payments measures by all contracting parties: i.e. that preference shall be given to the measure which has "the least disruptive effect on trade" while abiding by disciplines provided for in the GATT; that the simultaneous application of more than one trade measure for balance-of-payments purposes shall be avoided; and that whenever practicable, contracting parties shall publicly announce a time schedule for the removal of the measures.

V. Procedures for Consultations

12. The basic procedures under which consultations under Articles XII and XVIII(b) are carried out, including a "Plan of Discussion" for the consultations, were first laid down in 1958 (BISD, 7th Supplement, pp.90-98). Since then, they have been modified and adapted from time to time to meet changing circumstances and the exigencies of particular cases. The current procedures for "full" consultations, applying to all contracting parties, were established in 1970 (BISD 185/54). In 1972, the GATT Council also adopted procedures permitting "simplified" consultations
with developing countries consulting under Article XVIII:B. The new procedures were intended to preserve the legal requirements of the General Agreement and maintain opportunities for considering the balance-of-payments situation of developing countries invoking Article XVIII:B, while lessening the burden on the CONTRACTING PARTIES and on the consulting countries themselves.

13. Since the introduction in 1972 of simplified procedures for consultations under XVIII:B, the majority of consultations with developing countries have taken this form. Full consultations are held under XVIII:12(a) on new restrictions or an increase in the general level of restrictions, or under Article XVIII:12(b) if the Committee considers that the situation warrants them. In simplified consultations, the Committee is called upon only to recommend to the Council whether full consultations are desirable (20S/48 paragraph 3(c)). If it does so, the Committee is required to consult with the IMF and to prepare full consultations.

14. Since the entry into force of the 1979 Declaration, the material prepared for consultations consists of three basic documents: (i) a "Basic Document" prepared by the consulting country in case of a full consultation, or a "Written Statement" prepared also by the consulting country in case of a simplified consultation; (ii) a "Background Paper"

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6 The 1979 Declaration (paragraph 8) introduced five non-exclusive criteria for the decision to hold full consultations: (a) the time elapsed since the last full consultations; (b) the steps the consulting contracting party has taken in the light of conclusions reached on the occasion of previous consultations; (c) the changes in the overall level or nature of the trade measures taken for balance-of-payments purposes; (d) the changes in the balance-of-payments situation or prospects; (e) whether the balance-of-payments problems are structural or temporary in nature.

7 The Basic Document for a full consultation under Article XII:4(b) or XVIII:12(b) covers the following points: legal and administrative basis of the import restriction; methods used in restricting imports; treatment of imports from different sources including information on the use of bilateral agreements; commodities, or groups of commodities, affected by the various forms of import restrictions; state trading, or government monopoly, used as a measure to restrict imports for balance-of-payments reasons; measures taken since the last consultation in relaxing or otherwise modifying import restrictions; effects of the import restriction on trade; general policy in the use of restrictions for balance-of-payments.
prepared by the GATT secretariat;™ and (iii) a "Recent Economic Developments" document prepared by the IMF.

15. The "Plan of Consultations" for full consultations under Articles XII and XVIII:B, established in 1970 (BISD 18S/48) contains four main elements:

(a) Balance-of-payments position and prospects
(b) Alternative measures to restore equilibrium
(c) System and methods of restrictions
(d) Effects of restrictions

Within each main element, the plan lays down guidelines for the aspects to be covered." Since 1983, the Committee has also, if a consulting developing country requests it, paid special attention to factors relating to "the possibilities for alleviating and correcting the balance-of-payments problem through measures that contracting parties might take to facilitate an expansion of the export earnings of the consulting contracting party" (1979 Declaration, paragraph 12).

16. Under the first heading of "Balance-of-Payments position and prospects" the plan of consultation outlines six suggested topics: the balance-of-payments situation and level of monetary reserves; balance of payments prospects and expected movements in reserves; special factors affecting the availability of or the need for monetary reserves; factors, either external or internal, affecting the various elements of the balance of payments, such as exports or imports; effects of the restrictions on the balance of payments and expected duration of the restrictions; and prospects of relaxation or elimination and likely effect of such action on the balance of payments. "External" factors touched on under this heading...
have included the effects of major exchange rate fluctuations on trade prospects (in particular, effects of the wide fluctuations which have taken place in the international value of the U.S. dollar), the extent of foreign indebtedness of the countries under consultation and the burden of debt servicing.

17. The second heading "Alternative measures to restore equilibrium" contains three sub-headings: internal monetary and fiscal situation and other relevant matters which may affect the balance of payments; internal action to preserve or restore equilibrium, including long-term measures such as those designed to raise productivity and export capacity or to reduce structural disequilibrium or rigidities; and other measures which may help to restore the country's balance of payments. It thus concentrates heavily on domestic macro-economic policy questions as well as measures aimed at increasing productivity and export competitiveness. The depth of discussion under this heading has leaned heavily on the information provided by the IMF in its "Recent Economic Developments" papers and statements to the Committee. The types of domestic measures touched on in this context have included budgetary, exchange rate and monetary policies; policies adopted to control inflation; industrial licensing and production controls; adjustment policies pursued under IMF stand-by programmes or under structural adjustment lending by the World Bank, as well as pricing, subsidization and incomes policies.

18. The third heading, "System and methods of the restrictions" covers four aspects: the legal and administrative basis of the restrictions, methods used in restricting imports, treatment of imports from different countries or currency areas, and the use of State trading or governmental monopolies in imports and the restrictive operation, if any, of such regimes. The fourth, "Effects of the restrictions", covers protective effects of the restrictions on domestic production and difficulties or hardships that may be expected upon relaxation or elimination of the restrictions. It also covers steps taken to reduce incidental protective effects of the restrictions and to minimise the difficulties of transition to the stage where balance-of-payments restrictions may be eliminated. Given the Committee's focus on trade measures taken for balance-of-payment purposes, questions relating to the system and methods of restrictions have been the most detailed area of the discussions.

VI. Rôle of the International Monetary Fund in Consultations

19. Consultations between the GATT CONTRACTING PARTIES and the IMF, pursuant to Article XV:2 of the General Agreement, take place in the Balance-of-Payments Committee 'prior to the GATT consultations', through a statement delivered by the IMF representative on behalf of the Fund's Executive Board. Such a statement is only made in full BOP consultations. As noted above, the Fund also supplies material for full and simplified consultations through "Recent Economic Developments" papers resulting from IMF missions to consulting countries. These are circulated to members of the Balance-of-Payments Committee as soon as possible after they are received.
20. The conclusions of the IMF statements may include a judgement on whether the level of restrictions is within the bounds necessary to stop a serious decline in the country's monetary reserves or contain a deterioration of the balance of payments. Fund statements for balance-of-payments consultations also focus on the macroeconomic adjustment, financial and monetary policies being pursued by the consulting country.

VII. Reports of the Committee to the GATT Council

21. All elements of the Committee's reports are agreed by consensus, but it is natural that the conclusions of full consultations should be most closely scrutinized by the consulting countries and other participants in the consultations. Reports on all consultations in the Balance-of-Payments Committee are submitted to the Council for discussion and adoption. The Council's adoption of the reports, which are introduced by the Chairman of the Committee, gives effect to the recommendations of the Committee.

22. In full consultations, the Committee may determine whether or not the trade measures are justified under Articles XII or XVIII:B (as applicable). It may also make recommendations concerning the desirability of modifying the type or level of the trade measures or the establishment of a timetable for liberalization of the measures.

23. The Committee's recommendations have varied according to its view of the severity of the situation of particular consulting countries or of the extent to which it considered that the direction of policies conformed with the norms set out in the General Agreement. The Committee has also on occasion said that it would keep the evolution of measures under review or urged the consulting country itself to review measures periodically with a view to their reduction or elimination.

24. The Committee's conclusions have often addressed domestic adjustment measures and the importance of external factors in balance-of-payments problems. Regarding domestic adjustment, reference has on occasion been made to the views of the IMF. In recognizing external economic factors, reference has been made at various times to the course of world market

11. The opinion of the IMF concerning the balance-of-payments justification for restrictions can be a major influence on the Committee's conclusions. For example, in 1973, the Committee based its finding that "balance-of-payments provisions, under Articles XII and XVIII:B, were no longer applicable in the case of Spain" directly on the finding of the IMF and the provisions of Article XV:2 of GATT. In the recent case of Korea, the IMF considered that the balance of payments situation did not justify the restrictions maintained by Korea. The Committee was not required to reach a firm conclusion since Korea undertook to phase out its remaining restrictions within an agreed timetable.
prices, the effects of global economic recession, difficulties of external financing, the effects of drought and floods, and the existence of a number of external factors beyond the control of the authorities. One of the elements to which the Committee has given most significance in its conclusions has been the question of the temporary nature of balance-of-payments trade measures, and the length of time measures have been maintained by consulting countries.

25. All reports by the Committee are adopted by the GATT Council. In many cases the reports have been adopted without discussion. However, from time to time reports have been discussed in the Council, often upon initiation by the country which is the subject of the report. On a number of occasions contracting parties, while not opposing the adoption of reports, have used Council discussion to express regret at the continued maintenance of import restrictions and to press for faster or more complete liberalization. In some cases, countries have also reserved their GATT rights in relation to measures which they saw as damaging their interests and whose maintenance they believed not to be in conformity with GATT.

26. Extensive discussions in the Council, particularly since 1984, have addressed the effects of the external economic environment on the balance-of-payments position of consulting countries. Broadly speaking, these discussions have been of two kinds: those on the general macroeconomic environment, including the impact of recession and especially the burden of debt and debt-servicing; and those concerning the trading environment, and particularly the market access conditions, confronting consulting countries. The Council has also held discussions of a more general kind on the balance between the obligations of developed and developing contracting parties in the matter of surveillance of their trade policies.

B. ARTICLE XIV (Exceptions to the Rule of Non-Discrimination)

27. Article XIV permits a contracting party which is invoking Article XII or XVIII:B to apply quantitative restrictions discriminatorily under certain circumstances. These circumstances were envisaged in the light of immediate post-war economic conditions and institutional arrangements, when the currencies of many developed countries were inconvertible. Since 1961, no contracting party has notified the CONTRACTING PARTIES that it is availing itself of the provisions of Article XIV. However, Article XIV:1 may still have relevance as a means of avoiding any legal inconsistency between the IMF and GATT disciplines over the discriminatory use of restrictions.

28. The circumstances foreseen in Article XIV that could justify the use of discriminatory quantitative restrictions are defined in paragraphs 1 and 5(a). These provisions permit discriminatory restrictions of "equivalent effect" to restrictions on payments and transfers for current international transactions applied and approved (or which the Fund is prepared to state could have been applied and would have been approved) under IMF Articles VII:3(b), VIII or XIV, or under analogous provisions of a special
exchange agreement entered into under Article XV:6 of the General Agreement. IMF Article VII:3(b), the only explicit indication in the IMF's Articles of when the discriminatory application of exchange restrictions or currency practices might be justified, applies only when the IMF has designated a currency as "scarce". As this has never happened, this justification for discriminatory quantitative restrictions under GATT Article XIV:5(a) has never been available to any contracting party.

29. IMF Articles VIII and XIV are not explicit about what circumstances might justify the discriminatory application of restrictions, and consequently neither is Article XIV:1 of the General Agreement beyond the fact that the restrictions must be for balance-of-payments purposes. The Fund does not make information publicly available on whether countries have been authorized to use discriminatory exchange restrictions or currency practices under Article XIV of the IMF, or on whether they have used them under Article VIII of the IMF subsequent to their becoming member countries. Article XIV of the General Agreement does not call on the CONTRACTING PARTIES to inform themselves of the IMF's decisions in this regard unless a contracting party applies discriminatory quantitative restrictions. Paragraph 1 of Ad Article XIV notes that the nature, effects and reasons for discrimination in import restrictions can be examined in Balance-of-Payments Committee consultations.

C. ARTICLE XV (Exchange Arrangements)

30. Article XV is almost identical to the corresponding Article 24 of the Havana Charter, which bore the more explicit title of "Relationship with the International Monetary Fund and Exchange Arrangements". Most provisions of Article XV have a direct bearing on the treatment of balance-of-payments problems in the GATT. The basic purpose of the Article is to respond to the evident interlinkages and substitutability between measures taken in the trade and monetary fields, by providing for co-operation between the CONTRACTING PARTIES and the International Monetary Fund in order that they "may pursue a co-ordinated policy with regard to exchange questions within the jurisdiction of the Fund and questions of quantitative restrictions and other trade measures within the jurisdiction of the CONTRACTING PARTIES (XV:1). Contracting parties "shall not, by exchange action, frustrate the intent of [the GATT] nor, by trade action, the intent of the provisions of the Articles of Agreement of the IMF" (XV:4). If the CONTRACTING PARTIES consider at any time that exchange restrictions on payments and transfers in connection with imports are being applied by a contracting party in a manner inconsistent with the exceptions provided in the GATT for quantitative restrictions, they shall report thereon to the Fund (XV:5). However, "nothing in this Agreement shall preclude" the use of exchange controls consistent with IMF rules or the use of trade controls to make these effective (XV:9(a) and (b)).

31. In all cases of consideration of balance-of-payments questions, the CONTRACTING PARTIES are required to "consult fully" with the IMF (see paragraph 22 above) . They are required to accept all findings of "statistical and other facts presented by the Fund relating to foreign
exchange, monetary reserves and balances of payments" and the Fund's
determination as to whether exchange action by a contracting party is in
accordance with IMF Articles VIII or XIV. Moreover, the CONTRACTING
PARTIES shall accept the Fund's determination as to "serious decline",
"very low level", or "reasonable rate of increase" in monetary reserves,
(Article XV:2).

32. Further provisions aimed at ensuring that there is no conflict between
the provisions of GATT and the Articles of Agreement of the IMF are
contained in Article XV, paragraphs 4 and 5. Contracting parties are
required not, by exchange action, to frustrate the intent of the provisions
of GATT, nor by trade action, the intent of the Fund's Articles of
Agreement (XV:4). Moreover, if the CONTRACTING PARTIES consider at any
time that exchange restrictions on payments and transfers in connection
with imports are being applied by a contracting party in a manner
inconsistent with the exceptions in GATT regarding quantitative
restrictions, they shall report upon to the Fund.

33. The 1955 review session agreed that "paragraph 9(a) was not to be
interpreted so as to preclude the CONTRACTING PARTIES from discussing with
a contracting party the effects on the trade of contracting parties of
exchange controls or restrictions imposed or maintained by that contracting
party, or from reporting on these matters to the IMF (as was specifically
envisaged in paragraph 5 of the Article)". The IMF Executive Directors, by
contrast, decided in 1960 that, for the purposes of IMF Article VIII, the
criterion for distinguishing between trade and exchange measures should
normally be the technique used. Many countries have regulated payments for
imports through exchange control measures or by a combination of exchange
and trade measures. The exchange measures as such have not generally been
discussed in the Balance-of-Payments Committee. However, the trade effects
of exchange restrictions have been discussed in the Committee, e.g. in the
case of Italy in 1981.

34. Article XV includes three paragraphs to meet the situation of a
contracting party which is not a member of the IMF. Paragraph 6 of Article
XV requires that a contracting party which is not a Fund member must within
a stipulated period (fixed by a 1949 Resolution at a maximum of four months
after accession to GATT) either join the Fund or enter into a special
exchange arrangement with the CONTRACTING PARTIES, which becomes part of
that government's GATT obligations. Similarly, a contracting party which
withdraws from the Fund must forthwith enter into a special exchange
agreement with the contracting parties. The aim of such an agreement is to
"provide to the satisfaction of the CONTRACTING PARTIES that the objectives
of [the GATT] will not be frustrated as a result of action in exchange
matters by the contracting party in question" (XV:7(a)). The obligations
imposed in exchange matters on the contracting party by any such agreement
are not to be generally more restrictive than those imposed on Fund members
by the IMF's Articles. Contracting parties which are not Fund members are
to furnish such information within the general scope of IMF Article VIII:5
as the CONTRACTING PARTIES may require in order to carry out their functions under the GATT.\textsuperscript{12}

\textsuperscript{12}Section 5 of IMF Article VIII authorizes the Fund to require its members to provide national data on gold and foreign exchange holdings, exports and imports, balance-of-payments, international investment, national income, prices, exchange rates, exchange controls, etc.