

FACULTY OF JURIDICAL SCIENCES

Lecture-2



HISTORICAL BACKGROUND

The General Agreement on Tariffs and Trade (GATT), the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development (IBAD) were established to provide institutional framework for post-War international economic order. They were planned as response to economic problems that afflicted international economy during inter-War period. Soon after the First World War, the League of Nations was established to foster multilateral approach towards international problems. Though the League did not have a separate set up to deal with international economic problems, its Secretariat made significant intellectual contribution to the analysis of economic problems. The first World Economic Conference was held under the under the League's Auspices in 1927; and it produced Geneva Convention on Import and Export Prohibitions. This was the first multilateral effort to establish a legal regime for international trade. The Convention prohibited quantitative restrictions on international trade except for balance of payments purposes. Though it was signed by large number of states, there was no adequate ratification. Hence it did not come into force.

In the early 1930s, international economy was hit by the Great Depression. States reacted by imposing restrictions on incoming goods, hoping that they would thereby protect domestic employment. The U.S. Congress passed Smoot-Hawley Act in 1930 whereby import duties were raised considerably. Other states reacted in the same way; and beggar-my-neighbor policy became the order of the day. Between 1929 and 1934, international trade shrank by 2/3.

When the USA realized that it could not sell its products any longer in international market, it tried to get out of it by concluding bilateral trade agreements with other countries whereby the parties mutually reduced the tariffs on selected products. The U.S. Congress passed Reciprocal Trade Agreements Act in 1934, authorizing the President to conclude bilateral trade agreements for certain period of time; and when that time expired, it renewed the authority a couple of times. The fast track authority, so given to the President was used by the latter to enter into the GATT.

The U.S.A. concluded a number of reciprocal trade agreements with other countries. All of them invariably contained so-called conditional most favored nation clause. For example, country A would give most favored nation treatment to certain goods coming from B provided B reciprocates this gesture. Thus both A and B would extend to each other most favored nation treatment on reciprocal basis. But this kind of bilateral approach had its own limitations. Thus when the countries started negotiations for the establishment of International Trade Organization, there was general consensus on multilateral approach based on unconditional most favored nation treatment.

In 1939, the Second World War broke out. Many scholars are of the view that economic misery, caused by the Great Depression facilitated the rise of totalitarianism in Germany and Italy. The Allied Powers fought the War against the Axis Powers under the slogan of protecting democracy

from the onslaught of totalitarianism. Even as the War was raging, the Allied Powers started the deliberation on new World order which would secure the World peace. The Atlantic Charter, agreed between the USA and the UK, was the first step in this direction; and this Charter, inter alia, emphasized free trade. Free trade among free people was the guiding ideology for the reconstruction of war-ravaged world. The United Nations Organization was established in 1945 to advance the cause of human rights and fundamental freedoms. Free trade which is the expression of economic freedom was considered as the fortification of liberal world order. As Cordell Hull, the leader of the U.S. delegation to the ITO negotiations put it:

Enduring peace and welfare of nations are indissolubly connected with friendliness, fairness, equality and maximum degree of freedom in international trade. Unhampered trade dovetails with peace and high tariffs, trade barriers and unfair competition with War.

By the end of 1945, the U.N.O., the IMF and the IBRD came into existence. The negotiations for the International Trade Organization (ITO), the trade component of post-War international economic order, started in 1946. The Economic and Social Council passed a Resolution, on the initiative of the U.S.A., convening a U.N. Conference on Trade and Employment. A Preparatory Committee, consisting of 19 countries, was set up to prepare the background materials for the proposed Conference. A U.S. proposal with inputs from the U.K. on International Trade Organization provided the basis for the deliberation of Preparatory Committee. The Preparatory Committee held 3 meetings: in London in October, 1946; in New York in January, 1947 and in Geneva during April-October, 1947. The final U.N. Conference on Trade and Employment was held during November 1947 and March 1948 and it produced the U.N. Convention on Trade and Employment, popularly known as Havana Charter.

The main interest of the U.S.A. in ITO negotiations was the opening up of markets for its surplus products. It insisted on parallel negotiations for the reduction of tariffs. Given the prominence of the U.S.A., other countries could not resist this demand. In Geneva meeting, 45000 tariff concessions worth \$ 10 billion were negotiated between 23 countries. 1947 was a crucial year for the negotiators. The U.S.A. realized that the negotiations for the ITO were moving much against its ideas; and hence there would be a likelihood of stalemate. Further, by the end of 1947, the fast track authority, given to the President under the Reciprocal Trade Agreements Act, would expire; and it was unlikely that the Congress would extend this fast track authority, given its hostility towards free trade policies in general. Under these circumstances, the U.S. delegation took out certain portions of the ITO charter in making, especially from Part IV dealing with "Commercial Policies" and produced the General Agreement on Tariffs and Trade (GATT) in order to provide the legal backing to the tariff concessions already negotiated in Geneva meeting and also to provide a legal framework for future negotiations. The expression "Tariffs" in the title "The GATT" indicates the main concern of the U.S.A in undertaking this exercise.

The GATT was essentially conceived as a stop-gap arrangement pending the establishment of the ITO. Article XXIX of the GATT dealing with the relation between the GATT and the

proposed Havana Charter makes this point clear. Therefore, the participant states thought of adopting the GATT provisionally through a protocol. Accordingly, a Protocol on Provisional Application was drafted, and the idea was that by accepting this Protocol, the GATT would be operational. The Protocol contained two important provisions:

1. Part I and III of the GATT shall be accepted by all the Contracting Parties
2. Part II of the GATT shall be accepted “to the fullest extent not inconsistent with existing legislation.

The Protocol also provided in its Preamble that the GATT would “apply provisionally on and after 1st January 1948” provided the following eight Governments sign the Protocol not later than 15 November 1947. These eight Governments were: Australia, Belgium, Canada, France, Luxembourg, Netherlands, the U.K. and the U.S.A. All of them signed before 15 November 1947. Many other countries joined the GATT later on.

Part I of the GATT consisted of Articles I and II providing for most favored nation treatment and the Schedule of Concessions. Part III, consisting of Articles XXIV to XXXV, mainly dealt with procedural issues including Tariff Negotiations, i.e. Article XXVIII Part II of the GATT consists of substantive obligations such as national treatment, trade remedies, quantitative restrictions etc. The interpretation of the clause in the Protocol: “the fullest extent not inconsistent with existing legislation” was controversial even at that time. It was popularly called as “grand father clause” in the sense that it protected the existing rights of states. But a contracting state is prevented from enacting legislation contrary to the GATT once it chooses to become a party to the GATT.

As was expected, there was strong opposition to the Havana Charter in the U.S. Senate. The general impression in the U.S.A. was that it had imposed heavy burden on the U.S.A. to salvage the Europe from economic crisis. Meanwhile, the control of the U.S. Congress passed from the hands of Democrats to Republicans while the Presidency was still with Democratic Party. Sensing the defeat in the Senate, the President in 1950 withdrew the bill containing Havana Charter. And with that, the post-War deliberations to establish a new economic order came to an end.