

Implementing the Sensitive Products Provision on the Basis of an Additional Pro-Rated TRQ Commitment for Non-Compliance with the General Tariff Cut Formula¹

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The July Framework includes a provision for “sensitive” products which would be subject to more favourable treatment as regards tariff cuts. The related provisions read as follows (paras 31 to 34 of the July Framework):

“Sensitive Products

Selection

31. Without undermining the overall objective of the tiered approach, Members may designate an appropriate number, to be negotiated, of tariff lines to be treated as sensitive, taking account of existing commitments for these products.

Treatment

32. The principle of ‘substantial improvement’ will apply to each product.

33. ‘Substantial improvement’ will be achieved through combinations of tariff quota commitments and tariff reductions applying to each product. However, balance in this negotiation will be found only if the final negotiated result also reflects the sensitivity of the product concerned.

34. Some MFN-based tariff quota expansion will be required for all such products. A base for such an expansion will be established, taking account of coherent and equitable criteria to be developed in the negotiations. In order not to undermine the objective of the tiered approach, for all such products, MFN based tariff quota expansion will be provided under specific rules to be negotiated taking into account deviations from the tariff formula.”

The issues in brief

The demandeurs of including a sensitive products provision in the new AoA have been typically developed country Members on the basis of non-trade concerns and other considerations. By and large sensitive products are thought to be those products that enjoy a high degree of protection in some developed countries, both in terms of domestic support and border measures (high bound and applied tariffs). However, the Framework text does not limit the applicability of this provision to developed country Members only. All Members (developed and developing) would be eligible to use such a provision, although developing countries would have to contemplate the pros and cons of making use of this provision vis-à-vis the Special Products provision to which they would have exclusive access on an SDT basis.

¹ This Note is part of three notes on approaches to implement certain market access provisions of the July Framework. The other two notes are:

- *Implementing the Special Products (SPs) Provision on the Basis of an Aggregate Deviation from the General Tariff Cut Formula*
- *Implementing the Special Safeguard Mechanism (SSM) on the Basis of a Maximum Contingency Levy*

² The views expressed in this paper are those of the author and do not necessarily reflect official policy of the Food and Agriculture Organization.

The provision on sensitive products is under the market access pillar of the Framework text and as such the differentiation that would be made on such products would apply to the level of tariff cuts compared to what would have been required from the application of the general tariff cut formula. Although explicit discussions on the sensitive products provision came late in the negotiations leading to the July Framework, issues that have been raised include the number of products that may be designated as sensitive, the degree of protection that would be afforded (i.e. by how much they would deviate from the generally applicable tariff cut formula), and the additional commitments that these Members will have to make for a more favourable treatment of these sensitive products³.

Proponents of sensitive products seek maximum flexibility in the modalities of this provision as regards the number of products to be designated as sensitive, the degree to which they would be protected from tariff cuts and the TRQ they would be required to offer in lieu of this derogation. Others see the sensitive products provision as an important barrier to developed country markets and wish to minimize its adverse effect on market access.

An approach based on an additional pro-rated TRQ commitment for non-compliance

The Framework text is explicit about the way that a 'substantial improvement' on market access is to be achieved for sensitive products, i.e. through combinations of tariff quota commitments and tariff reductions applying to each product. The text also states that TRQ expansion will be provided under specific rules to be negotiated taking into account deviations from the tariff formula. This basically provides the main ingredients of an approach that could be followed, namely that the greater the deviation from formula cuts of those products designated as sensitive, the greater the price that has to be paid in the form of a higher TRQ commitment.

A way to implement the essence of what is described in the Framework text is by quantifying non-compliance with the generally applicable tariff cut formula. This is illustrated in Figure 1 where the actual tariff cut for product x is less than the required cut as expected by the application of the general tariff cut formula. The difference between the required cut and the actual cut is the absolute measure of non-compliance with the general tariff cut formula, for the product in question. The relative degree by which the tariff cut for product x does not comply with the general formula can be defined as the non-compliance ratio:

$$\text{Non-compliance ratio} = (\text{Required cut} - \text{Actual cut}) / (\text{Required cut})$$

Full compliance (actual cut is equal to the required) would imply a non-compliance ratio of 0 and this would be the case for products other than sensitive. For sensitive products the non-compliance ratio will be somewhere between 0 and 1, the latter value corresponding to the case where there was no reduction at all to the initial bound tariff of the product in question.

The other element that is needed to implement the sensitive products provision is the maximum additional TRQ commitment (a level to be negotiated – see below) for making no effort to comply with the general tariff cut formula applicable to other products.

With these two elements, the additional TRQ obligation for sensitive products would amount to the non-compliance ratio times the maximum additional TRQ commitment. To illustrate how this may work in practice, assume that the maximum additional TRQ is 10% (Table 1). For sensitive product 1, the Member in question reduced its bound tariff by 15 percentage points (from 70% to 55%), however still above the required cut of 20 percentage points (resulting from the generally applicable tariff cut formula). This would imply a non-compliance ratio of 0.25 and therefore the additional TRQ for that product would be 2.5% (=0.25*10%). For the last (nth) product in Table 1 the non-compliance ratio is 0.75 and therefore this would necessitate an additional TRQ commitment of 7.5% (=0.75*10%) for that product.

³ Unlike the provision of Special Products, countries opting for sensitive products will have to offer an expansion in TRQ as stipulated in para 34 of the Framework text.

What needs to be negotiated

The sole parameter that needs to be negotiated to implement the sensitive products provision according to the approach proposed here is the maximum TRQ commitment for non-compliance.

One issue that could be raised in this regard is whether this maximum TRQ commitment should be differentiated according to countries and products or it should be uniform across the board. Differentiation for developing country Members on SDT basis is on weak grounds in this case given that these countries have also exclusive access to the Special Products provision which would not require any additional TRQ commitment for products designated as SPs.

Second, as regards differentiation between products, a case could perhaps be made for a lower TRQ commitment for products with already low initial bound tariffs compared to those with high initial bound tariffs. However, while the trade distorting effect of a high tariff is greater than that of a lower tariff, it could be argued that the concern here is not to “penalize” a member for where it stands in the tariff scale but for not making an effort to comply with the generally applicable tariff cut rules. In fact, it is likely that the adjustment required for products with high bound tariffs would be greater than that of products with low tariffs⁴. Therefore, a greater “penalty” for higher tariffs would already be built-in in the generally applicable tariff cut formula.

In view of these considerations, negotiation of a uniform maximum TRQ commitment for non-compliance, applicable across the board for all products and countries is suggested. The applicable TRQ would be pro-rated according to the degree of compliance for individual products. Also, if at any time during the implementation period the Member concerned decides to comply fully with the formula cut for a particular product, the related TRQ for that product will cease to apply.

Further considerations and implications

An additional issue that requires consideration is whether there would be compensation from other products (i.e. tariff cuts in excess of what is required by the generally applicable formula) to make up for the reduced tariff cuts for sensitive products. This may be necessary if there is a provision in the new agreement on market access which stipulates a minimum overall average reduction commitment for each Member over all products. To the extent that tariffs for some products are reduced by less than what is required by the general tariff cut formula (those designated as sensitive), other products will have to be cut by more.

It may be argued that Members opting for a certain number of sensitive products have already paid a price for that derogation in the form of the additional TRQ. However, some compensation (even partial) by greater cuts in other products could create desirable dynamics in order to limit the use of the sensitive products provision. This is because the trade-offs from protecting certain products will become more transparent (other products would be affected) and this is likely to result in very important debates and decision making processes at the national level as to why certain products are sensitive and what are the implications for other products for a disproportional protection of such sensitive products.

⁴ This is evident from para 29 of the July Framework which states that “Progressivity in tariff reductions will be achieved through deeper cuts in higher tariffs with flexibilities for sensitive products. Substantial improvements in market access will be achieved for all products.”

Figure 1. Non-compliance ratio used in the additional pro-rated TRQ

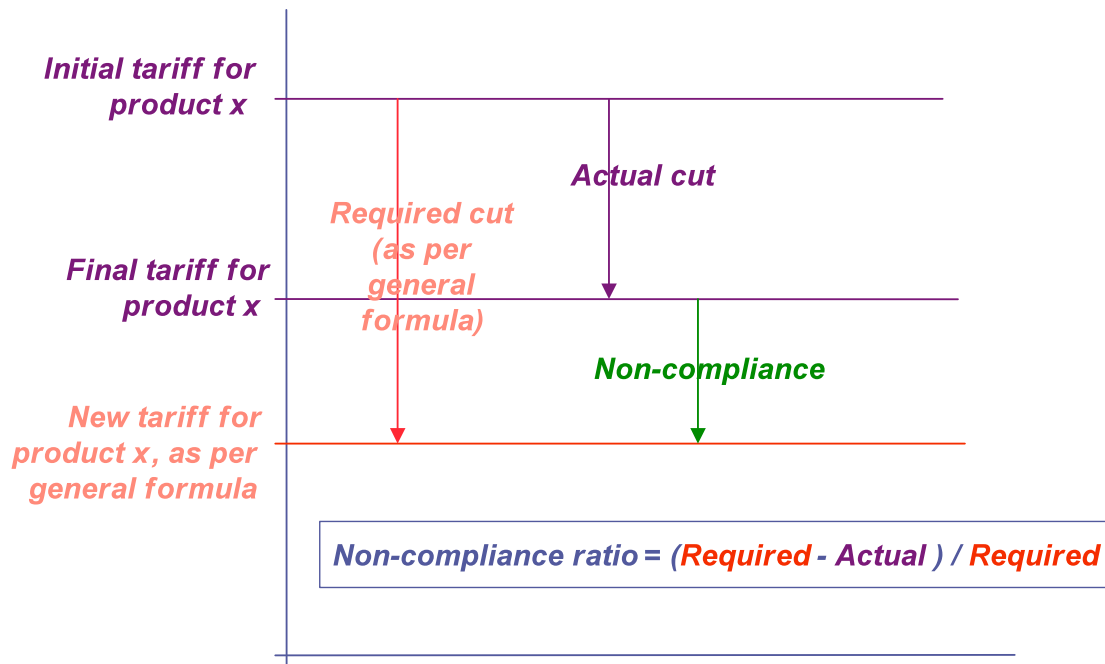


Table 1. Calculation of the additional pro-rated TRQ for non-compliance

Sensitive product	(1) Initial bound tariff (%)	(2) Tariff cut resulting from the generally applicable formula (percentage points)	(3) Actual tariff cut (percentage points)	(4) Non-Compliance ratio ^{1/} (%)	(5) Additional TRQ for non-compliance ^{2/} (%)
1	70	20	15	0.25	2.5
2	250	150	100	0.33	3.3
n	100	40	10	0.75	7.5
^{1/} the ratio between (2)-(3) over (2) ^{2/} residual non-compliance times the maximum penalty (10% additional TRQ was assumed – an across-the-board level, to be negotiated).					