CHAPTER 9

SAFEGUARDS AND EXCEPTIONS

VIRTUALLY all international trade agreements or arrangements contain safeguard provisions and exceptions. Broadly defined, the term 'safeguard protection' refers to a provision permitting governments under specified circumstances to withdraw—or cease to apply—their normal obligations in order to protect (safeguard) certain overriding interests. Safeguard provisions are critical to the existence and operation of trade-liberalizing agreements, as they function as both insurance mechanisms and safety valves. They provide governments with the means to go back on specific liberalization commitments—subject to certain conditions—should the need for this arise (safety valve). Without them, governments may refrain from signing an agreement that reduces protection substantially (insurance motive). This chapter focuses primarily on the safeguards and exceptions embodied in the GATT. Those of the GATS are either very similar or still in an embryonic stage. Safeguard provisions in the agreement on TRIPS are discussed in Chapter 8.

The various provisions of the WTO in this area can be separated into two categories. The first are those that can be used in the event of the occurrence of a predefined set of circumstances, which legitimize temporary increases in import barriers. The second constitute permanent exceptions to the general obligations. The first category can be further divided into those dealing with so-called unfair trading practices (exports that are dumped or that benefit from actionable subsidies) and those that can be applied without having to demonstrate 'unfairness' on the part of trading partners. For the latter, the trigger solely concerns economic circumstances in the importing country. Many of the provisions allowing for temporary imposition of protection that are not in response to 'unfair' trade can give rise to claims for compensation by affected exporting nations.

Provisions that allow for the *temporary* suspension of obligations include:

Antidumping (AD): measures to offset dumping—pricing of exports below what is charged in the home market; foreign pricing below costs of production; or foreign pricing below what is charged in a third market—that materially injures a domestic industry (Article VI GATT).

Countervailing duties (CVDs): measures to offset the effect of subsidization that materially injures a domestic industry (Article VI GATT).

Balance of payments (BOP): restrictions on imports to safeguard a country's external financial position (Articles XII and XVIII:*b* GATT; Article XII GATS).

Infant industries: governmental assistance for economic development, allowing import restrictions to protect infant industries (Articles XVIII:*a* and XVIII:*c* GATT).

Emergency protection: temporary protection in cases where imports of a product cause or threaten serious injury to domestic producers of directly competitive products (Article XIX GATT).

Special safeguards: provisions embodied in the Agreements on Agriculture and Textiles and Clothing or in protocols of accession (in particular that of China) allowing for actions to be taken to restrict trade.

General waivers: allowing members to ask for permission not to be bound by an obligation (Article IX WTO). In contrast to the other mechanisms, this requires formal approval by the WTO Council.

Provisions allowing for permanent exceptions from general obligations include:

General exceptions: measures to safeguard public morals, health, laws and natural resources, subject to the requirement that such measures are nondiscriminatory and are not a disguised restriction on trade (Articles XX GATT; XIV GATS).

National security: allowing intervention on national security grounds (Articles XXI GATT; XIV*bis* GATS; 73 TRIPS).

Re-negotiation or modification of schedules: allowing for the withdrawal of concessions (bound tariff reductions or specific commitments) if compensation is offered to affected members (Articles XXVIII GATT; XXI GATS).

Only three of these provisions have an economy-wide rationale (balance of payments, general exceptions and national security). All the others are product/industry or issue/agreement-specific. All the industry-specific instruments are imperfect substitutes for each other: they all address the same issue, protecting domestic firms from foreign competition. In practice the balance-of-payments provision was often used by developing countries to protect specific industries, whereas industrialized countries have tended to use AD most frequently.

The GATS does not have provisions on contingent or infant industry protection, and an analogue to GATT Article XIX remains to be drafted (see Chapter 7). In large part this reflects the difficulty of applying these concepts to trade in services. The GATS does contain provisions allowing for actions to safeguard the balance of payments, for general exceptions and for re-negotiation of commitments. These

provisions are similar to those of the GATT, except that the language on modification of schedules differs from GATT by calling for mandatory arbitration if no agreement can be reached on compensation.

The rationale for safeguard instruments

The inclusion of some of the above provisions in a trade agreement is straightforward to understand. Government will want to be able to implement policies to achieve national security goals, pursue noneconomic objectives, and re-negotiate a deal *ex post*. They may also consider dumping or export subsidies to be unfair practices—although as discussed below it is not at all clear that these practices are inefficient (lower world welfare). What is perhaps less obvious is why the GATT (and other trade agreements) includes a safeguard provision. After all, if parties can re-negotiate, a safeguard procedure is redundant. In practice in the GATT years it did seem to be redundant as an Article XIX action was not that different from a re-negotiation—imposition of protection had to be accompanied by an offer of compensation for affected exporters. As discussed below, the result was that it was rarely used. Instead, countries used other instruments—including some that clearly violated GATT rules.

The rationale for a safeguard instrument can be understood in the context of the repeated game literature that analyzes the determinants of sustaining cooperation. If the short-term incentives confronting a government to cheat are not too large, but there are time periods where there is a politically driven need to deviate temporarily, a safeguard mechanism permits this to occur in a 'legal' and transparent way without giving rise to tit-for-tat retaliation and a breakdown of cooperation. If the need (incentive) is temporary, it makes little sense to engage in a re-negotiation. A temporary need to protect an industry might arise because governments need to slow down the adjustment to increased import competition to facilitate a more 'orderly' restructuring of an industry. Although the use of trade policy is likely to be inefficient in terms of fostering restructuring, it may be the only instrument to which a government has access.

Bagwell and Staiger (1990) and Horn, Maggi and Staiger (2006) provide another rationale for an escape clause: it provides governments with access to trade policy in periods in which there is high demand for imports, thereby avoiding the use of less efficient domestic instruments. In their analysis the presumed trigger is a (temporary) change in import volume that provides an efficiency (terms of trade) rationale for raising tariffs. Given that the source of the 'problem' is increased imports, a trade measure is most efficient.

Most scholars take the view that the prime reason trade agreements include safeguards is that this provides governments with some flexibility *ex post*, and that this encourages more cooperation in the negotiation phase. That is, they provide

insurance to governments—and import-competing industries—that if the result of liberalization is a level of imports that is hard to handle, protection can be re-imposed. In this view, the inclusion of a safety valve supports greater and deeper liberalization. As we will discuss below, there is some evidence for this view.

Use of safeguards and exceptions

The intent of the drafters of the GATT was that re-negotiation would be the primary mechanism to deal with a need for permanent rebalancing of concessions, and that Article XIX GATT would be used to grant temporary protection to industries finding it too difficult to confront increased import competition following negotiated liberalization (an MTN). The AD and CVD provisions were included in large part at the behest of the US, Canada and several European nations, which had such statutes on the books, although they were rarely used.

During the first 20 years of the GATT, re-negotiations and Article XIX were the major instruments used (Figure 9.1). Over time, however, industries in developed countries increasingly lobbied for VERs to obtain relief from import competition. Voluntary export restraints became a major instrument of protection in the 1970s because they provided some compensation for affected exporters, were

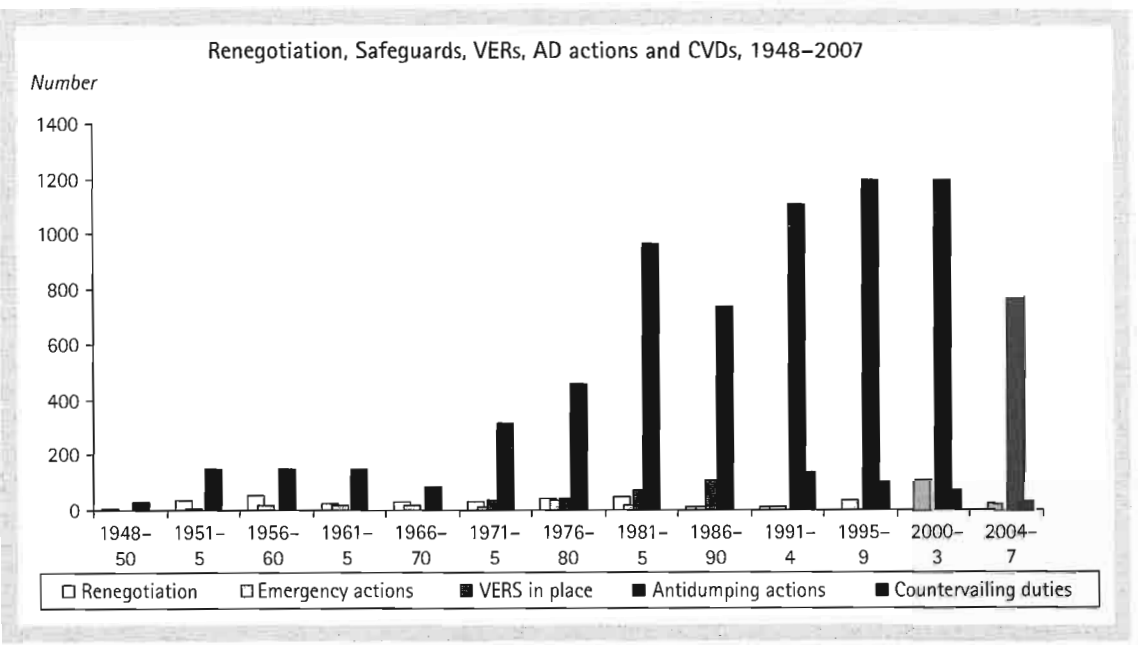

Fig. 9.1. Use of safeguard instruments, 1948–2007

Note: Data for antidumping and countervailing duties refer to investigations launched.

Sources: Finger (2001); Finger and Zlate (2005); Zanardi (2005); www.wto.org.

discriminatory, and were often directed against countries that did not have initial negotiating rights or principal supplier status (see Chapter 4). In the early 1980s, VERs covered some 10 per cent of world trade, with a trade-weighted average tariff equivalent on the order of 15 per cent (Kostecki, 1987). Although in absolute terms the number of VERs was relatively small, they often affected all the major suppliers and covered many product categories.

Starting in the mid-1970s the use of AD expanded substantially. Between 1980 and 1986, the EU imposed 213 AD actions, as compared to only 10 Article XIX measures. In the same period, the US imposed five Article XIX measures, as compared to some 195 AD actions (Finger and Olechowski, 1987). The revealed preference for AD and VERs reflected the fact that the conditions that needed to be satisfied to invoke Article XIX protection were relatively stringent. As discussed below, until this was changed in the Uruguay Round, Article XIX actions had to be nondiscriminatory and affected exporters had the right to compensation (or failing adequate compensation, could seek authorization from the GATT Council to retaliate). Governments preferred VERs and AD, as these instruments allowed them to discriminate across exporting countries and did not require (additional) compensation.

The total number of AD investigations rose steadily starting in the 1980s, with a dip in the late 1980s, reaching an all-time high of 309 in 2002. India, which adopted AD legislation in 1985 but only started to use the instrument in 1992 (following a major trade reform in 1991), initiated the most AD investigations in the 1995–2007 period (508), followed by the 'traditional' users of AD: the US (402), the EU (372), Argentina (222), and South Africa (205).[1] China is the leading target, having been at the receiving end of 597 investigations during this period.

There is often a cyclical aspect to the use of contingent protection. Once the wheels of international trade slow down, measures such as AD tend to increase. To invoke these instruments, business firms must be able to claim that they suffer injury from imports. Rapid economic growth in most parts of the world economy during 2003–6 led to a decline in the use of administered protection. As macroeconomic conditions deteriorate, it is safe to predict that an increasing number of AD cases will appear.

Up to the mid-1990s developing countries did not use the 'standard' instruments of contingent protection. Instead, they frequently invoked Article XVIII:*b* of the GATT to justify the use of QRs. If developing countries desired to impose tariffs they usually had significant leeway to do so because most had either not bound their tariffs or had bound them at high ceiling rates. In such cases countries are free to impose higher tariffs—there is no need to use AD or safeguards. Over time the invocation of Article XVIII:*b* as cover for the use of QRs by developing countries

[1] South Africa launched 211 cases in the 1948–58 period—by far the most intensive user of AD in the early GATT period (Zanardi, 2005).

declined, in part due to a shift towards more effective and efficient instruments to deal with BOP problems.

Table 9.1 provides a brief summary of the frequency with which various instruments have been invoked. Whatever the political rationale for safeguard instruments, their mere existence may reduce competitive pressure on domestic import-competing firms. They are also all inefficient, in the sense that the costs to

Table 9.1. Frequency of use of safeguard provisions

Instrument and GATT Article	Frequency of Use
Periodic—three year—renegotiations at the initiative of the country desiring to raise a bound tariff rate, Articles XXVIII:1 and XXVIII:5	1955–95: 207 instances 1995–2008: 24 instances (of which 12 re-negotiations still ongoing in October 2008)[a]
'Special circumstances' re-negotiations, Article XXVIII:4	1948–2008: 65 instances[b]
Waivers under GATT Article XXV	113 granted of which 44 still in effect in 1994 Between 1995 and 2007: 123 granted (including extensions)
Waivers under Article IX WTO	83 granted in the 2000–8 period
Withdrawal of a concession for infant industry purposes, Article XVIII:*a* and *c*	XVIII(a): 9 through September 2008 XVIII(c): 9 through September 2008
Measures by developing countries for BOP purposes, Article XVIII:*b*	Used by 16 countries at least once between 1959 and 2008
Emergency protection, Article XIX	1950–94: 150 actions (3.4 per year) 1995–2000: 49 investigations (9 per year) 2000–8 (June): 69 investigations (8.6 per year) 1995–2007: 83 measures imposed
Special safeguards under the ATC	1995–2005: 65 requests
Special safeguards, Agreement on Agriculture	Ten countries imposed actions in one or more years during 1995–2001 covering a total of 757 tariff lines (HS four-digit)[c]
Special safeguards against China under Protocol of Accession	21 investigations between 2002 and 2006;
Countervailing duties, Article VI	1985–2007: 522 initiations 1985–2007: 265 measures As of September 2008, more than 50 measures in force
Antidumping duties, Article VI	1995–2007: 3,200 initiations 1995–2007: 2,049 measures imposed About 1,300 measures in force as of September 2008

[a] Re-negotiations were minimal during 1995–2008 as tariffs were modified under rectification procedures or in the context of adopting the Harmonized System.
[b] Zero instances under the WTO during the 1995–2007 period.
[c] Data from G/AG/NG/S/9/Rev. 1.

Sources: Finger (2002); Bown (2008, 2009); WTO official documents and updates obtained from the WTO secretariat.

consumers are almost invariably larger than the benefits that accrue to the protected industry. In addition, industries can be expected to exploit substitution possibilities across instruments if these exist, making it more difficult for governments to control trade policy.

The various provisions allowing for protection under the GATT can undermine the liberalizing dynamic of the WTO, and limit the usefulness of the WTO to governments that seek insulation from protectionist lobbies. Governments (and their advisors) find it very difficult to sell the argument that it makes no economic sense to draft legislation which allows the various WTO provisions to be invoked. Invariably the response will be to point to the US, Canada or the EU—all active users of contingent protection. 'If they use it, why should we refrain' is a frequently heard argument. As a result, many developing countries have put in place the legal and administrative infrastructure to implement AD investigations. As a group, they have become the leading users of AD.

Views on the impact of contingent protection depend significantly on whether these measures are seen as 'facilitating devices', allowing liberalization to proceed, or as 'loopholes' that allow protectionist lobbies to reduce import competition and manage markets. The debate in this area is analogous to that arising on product standards: do they act more as barriers or are they catalysts for industrial upgrading and improving efficiency? Although there is general recognition that contingent protection plays an important political role, many exporters would argue there are excessive opportunities to re-impose protection. Economists also emphasize that some of the instruments that are legal under the WTO make no economic sense (antidumping in particular) as the underlying behaviour is not 'unfair', and are redundant from the perspective of being able to intervene for insurance or safety valve purposes.

9.1. Re-negotiation of Concessions

The GATT allows governments to re-negotiate tariff concessions and schedules (Article XXVIII). Re-negotiation centres on the compensation that must be offered as a quid pro quo for raising a bound rate. Under GATT rules, modification of schedules takes three basic forms: 'open season', which may be conducted every three years following a binding; 'special circumstances re-negotiations', which may take place when approved by GATT contracting parties; and 'reserved right re-negotiations', which may occur anytime during the three-year period following a binding if a notification is made by interested governments to that end (Dam, 1970).

Developing countries may follow a simplified procedure to modify or withdraw concessions. In negotiating the compensation required, account is taken of the interests of the country with which the concession was originally negotiated (which has so-called initial negotiating rights—INRs), the interest of the country having a 'principal supplying interest', as well as that of countries having a 'substantial interest'. Principal or substantial supplying interest requires a major or a sizeable share, respectively, in the market concerned, determined on the basis of import statistics for the last three years for which information is available.[2]

Countries having a substantial interest in the concession concerned (the negotiated tariff binding) have consultation rights only, whereas countries that have INRs or are principal suppliers, have negotiation rights. In disputed cases it is up to the Council to determine whether a given country is a principal supplier or whether it has a substantial interest. No such cases arose under GATT 1947. The main objective of the principal supplier rule is to provide for the participation in the negotiations, in addition to the country with the INRs, of countries with a larger share in the trade affected by the concession than the country with INRs might have. This allows a balance to be maintained between the old, previously negotiated situation and new trade patterns that emerge over time. Exceptionally, when the concession to be withdrawn affects trade that constitutes a major part of the total exports of a given country, the country may also enjoy principal supplier status (Article XXVIII: 1).

The Uruguay Round Understanding on the Interpretation of Article XXVIII enhanced the opportunities of affected exporters to participate in tariff renegotiations. The WTO member for which the relative importance of exports of the product on which a tariff is increased is the highest (defined as exports of the product to the market concerned as a proportion of the country's total exports) is considered to have a principal supplying interest if it does not already have so (or an INR) under GATT 1947 procedures. If no agreement is reached on compensation, affected countries may withdraw equivalent concessions.

Article XXI is analogous to the GATT renegotiation provision Article XXVIII, allowing for members to withdraw commitments after a three-year period has elapsed from the time that the commitment entered into force. The intent to modify must be notified to the GATS Council, and gives rise to compensation discussions. If agreement cannot be reached on compensation, the GATS provides for arbitration (no retaliation is allowed until the arbitration process has been completed). If the recommendations resulting from the arbitration are not implemented, affected members that participated in the arbitration may retaliate without needing authorization by the GATS Council. In this respect the GATS goes beyond GATT, which only provides for countries concerned to refer disagreements

[2] Principal supplying interest is determined with reference to the share in the export market; substantial supplying interest is determined in relation to a country's total volume of exports.

regarding compensation to the Council for Trade in Goods, who may in turn 'submit their views'.

The mechanisms for—and disciplines on—modification of tariff schedules are important. Before the completion of the Uruguay Round, on average re-negotiation of concessions occurred every year with respect to some 100 items, as compared to some 80,000 tariff lines bound. During the 1955–95 period, over 30 GATT contracting parties utilized the re-negotiation option more than 200 times (Table 9.1). To date, in the WTO period re-negotiations have been limited because adjustments have occurred in the context of adopting and implementing new versions of the Harmonized System (see Chapter 5). There were 24 re-negotiations under GATT Article XXVIII between 1995 and 2008, over half of which were ongoing at the time of writing.

In 2003, the EU indicated its intention to withdraw the tariff commitments listed in the Schedules of its ten new members (G/SECRET/20 and G/SECRET/20/Add.1). The issue was considered by the General Council throughout 2005 and 2006, as a result of the EU's nonrecognition of claims of interest submitted by Honduras and Guatemala in the consultations and negotiation process under Article XXVIII and XXIV GATT, as well as the entry into force of an EC-wide regime for bananas (2006). Consultations were being pursued at the time of writing with the aim of finding a satisfactory solution.[3]

9.2. Waivers

Tariff re-negotiations are limited in nature: by definition they only pertain to instances in which a country wants to raise tariffs above previously bound levels. Article XXV:5 GATT allows a member to request a waiver from one or more other obligations. Over 100 waivers were granted in the first 45 years of GATT history (Table 9.1), of which 44 were still in effect in 1994. From a systemic perspective, the waiver option allows members to obtain an exemption from a specific rule in situations where they might otherwise have been forced to withdraw from the agreement because of political imperatives at home. Waivers can be good or bad from an economic perspective. For example, a number of waivers were granted under GATT 1947 to countries allowing them to impose surcharges on imports for BOP purposes. Although this is an inferior instrument to deal with a BOP

[3] The status of re-negotiations is reported at www.wto.org/english/tratop_e/schedules_e/goods_schedules_table_e.htm

problem, at least it is better than the instrument called for by the relevant GATT provision—that is, QRs.

By far the most famous waiver was requested by the US in 1955. As noted in Chapter 5, QRs are allowed under Article XI of the GATT for agricultural commodities as long as concurrent measures are taken to restrict domestic production or to remove a temporary domestic surplus. Although it was the US that drafted this rule when negotiating the GATT, it proved too stringent for Congress, which did not wish to be bound by any international agreement and forced the Administration to ask for a waiver of this obligation in 1955. The waiver was necessary as existing US programmes supported domestic industries such as sugar and dairy without incorporating any incentives to reduce output. The root of the problem was Section 22 of the Agricultural Adjustment Act, which states that the Secretary of Agriculture must advise the President if he believes any agricultural commodity is being imported so as to interfere with Department of Agriculture price support programmes. Depending on the finding of an investigation into the matter, tariffs or QRs may be imposed. Because Section 22 violated GATT rules, US Administrations were reluctant to apply it. However, Congress had no such inhibitions, and amended Section 22 in 1951 to require the President to carry out its provisions regardless of international agreements, that is, the GATT (Evans, 1972: 72).

Under the WTO, disciplines on waivers were tightened. Article IX WTO allows waivers to be requested for any obligation imposed under a Multilateral Trade Agreement. Waivers under the WTO are time bound—in contrast to the GATT 1947—and are reviewed annually to determine if the exceptional circumstances requiring the waiver continue to exist. Any waiver in effect at the entry into force of the WTO was to expire by January 1997, unless extended by the WTO ministerial conference. Through 2006, 123 waivers were granted, including waiver extensions subsequent to annual reviews. Most waivers concerned technical issues related to the introduction of changes to WTO Schedules of tariff concessions following the adoption of the 2002 update of the HS. Politically important waivers concerned the nonapplication of Article 70.9 TRIPS to LDCs (see Chapter 8) for pharmaceutical products (until the end of 2015), EU preferences for the former Yugoslav republics (until 2011), the extension of Canada's waiver for its CARIBCAN preferential access programme (2011), the extension of a waiver for the Kimberley process (concerning certification schemes for rough diamonds to prevent trade in diamonds originating in conflict countries (2012) and the waiver for the ACP Cotonou convention (agreed at the Doha ministerial in 2001).[4] In addition, waivers have been granted in response to implementation concerns raised by developing countries, e.g. for customs valuation. As discussed in Chapter 5, a number of implementation matters were addressed by the relevant GATT committees.

[4] Information on waivers is reported in the WTO Annual Report (Section IV), which is available on the WTO homepage.

9.3. Emergency Protection (Safeguards)

Article XIX is GATT's general safety valve. It permits governments to impose measures to protect domestic producers seriously injured by imports. Designing a safeguard mechanism so that a balance is achieved between making it difficult to open the safety valve and avoiding an explosion of the boiler is not easy. The drafters of the GATT chose to be rather strict in this regard. Article XIX GATT states that necessary conditions included: (1) unforeseen developments; (2) resulting from the effects of obligations incurred by a contracting party (e.g. tariff concessions made in a MTN); (3) leading to increased imports; (4) that cause or threaten serious injury to domestic producers.

Safeguard measures were to be imposed on a nondiscriminatory basis. The interests of affected exporting countries were protected by a requirement that they be compensated. If no agreement was reached in consultations on compensation, an exporting country could be authorized to retaliate (suspend equivalent concessions or other obligations) against the safeguard-taking country. The compensation requirement made Article XIX a substitute for Article XXVIII renegotiation, the main difference being that the latter allows for a permanent change. Although Article XIX actions were supposed to be temporary in principle, no formal time limits were imposed. As a result some actions lasted for many years (Sampson, 1987).

The contracting parties to the GATT-1947 took only 150 official safeguard actions during the 1948–94 period (Table 9.1). Of these, only 20 led to (offers of) compensation—mostly in earlier years; retaliation occurred in 13 instances (GATT, 1994*b*). Article XIX was therefore used relatively infrequently. Reasons for this included the requirement that safeguard actions be nondiscriminatory (affect all exporters), a preference for QRs (much more difficult to implement in a nondiscriminatory manner than a tariff), the need to offer compensation, and the fact that in some jurisdictions (such as the US) granting of emergency protection is subject to the discretion of the President, who is required to take into account the impact of taking action on the economy. The relatively stringent conditions for obtaining Article XIX cover for protection reflected the fact that such protection violates earlier tariff commitments. This is not the case with AD or CVDs. As dumping or subsidization were agreed to be actionable, such measures are not a violation of tariff bindings as long the criteria laid out in the relevant GATT provisions are met. This helps to understand why over time AD came to be used increasingly as a de facto safeguard.

In addition to AD, discussed below, in the 1970s and 1980s VERs were used extensively to restrain exports of steel products and automobiles. Although

GATT-illegal (GATT, 1994*b*: 434)—with the exception of the MFA restraints, which had been sanctioned by the GATT—VERs did not give rise to formal dispute settlement cases. The reason was that no-one had an incentive to bring cases. Third country exporters, including the principal suppliers with which original tariff concessions on the goods involved had been negotiated, did not oppose VERs restricting their (new) competitors, and affected exporters tended to accept VERs because they allowed them to capture part of the rent that was created.

Instead of being confronted with an import tariff, the revenue of which is captured by the levying government, a VER involves a 'voluntary' cut back in export volume on the part of exporters. This reduction in supply will raise prices—assuming that other exporters do not take up the slack. Exporters therefore may get more per unit sold than they would under an equivalent tariff. Essentially they obtain what would be the quota rents if QRs were to be used (see Annex 2). There is a very large literature on VERs that will not be discussed here as VERs are now mostly of historical interest (see section 9.10).[5] The key points to remember about VERs are that they imply some direct compensation of affected exporters and that they selectively target exporters. Thus, they partially (and implicitly) satisfied GATT 1947 compensation requirements, while allowing for the circumvention of its MFN rule. The fact that VERs did not require import-competing industries to go through a formal process and satisfy the causality and injury standards that applied under Article XIX procedures made them particularly attractive for those seeking protection.

The specific criteria that are imposed in Article XIX were readily interpretable at the time, because the invocation of the instrument was tied to the specific commitments that GATT contracting parties had made in 1947. As argued by Sykes (2003), with the passage of time, the link to recently made concessions and 'unforeseen' developments made increasingly less sense. Implementing legislation in major traders such as the US did not mention the criterion that an import surge be linked to liberalization commitments and in practice countries simply required there to be a link between increased imports and serious injury.

This makes little economic sense. Imports are endogenous: they are determined by other factors and thus cannot be an independent source of injury to an import-competing industry. The quantity of imports will depend on the balance between domestic demand and supply in the importing country, and on the net demand and supply forces in the rest of world—which will determine the world market price for the good concerned. A variety of shocks that affect demand

[5] VERs have not disappeared completely. The EU for example, imposed what are effectively VERs in the context of bilateral agreements for steel exports with certain (non-WTO) transition economies, including Russia and the Ukraine, in 2003–4 (see Vermulst et al. 2004). Another example of new VERs was China's negotiated export limits to the US and EU in 2005 following the expiry of the ATC (discussed in Chapter 6).

and supply—such as changes in consumer tastes or the technology available to produce the good—will affect the market clearing world price, which in turn will determine the quantity imported into any given market. Although these considerations do nothing to undermine the political rationale for a safeguards instrument, they make it difficult for a government to determine whether 'imports' are actually the 'cause' of injury. A more economically justified approach would be to focus only the question of whether the import supply schedule has been affected, controlling for variables that affect domestic demand and supply—an approach that has been suggested by a number of economists (see Sykes, 2003). In practice, of course, trade may have little to do with the pressure for protection—generally the source of the problem is a lack of competitiveness of a given industry and a desire by a government to provide it with some 'breathing space'.

By the time the Uruguay Round was launched, the major objective of frequently targeted countries was to constrain the use of AD and VERs and to reassert the dominance of Article XIX in instances where the underlying problem was to address the pressure of import competition: the majority of cases. Two options were available: tighten the disciplines on the use of VERs and AD, or, alternatively, reduce the disincentives to use Article XIX. Both approaches were pursued. Little progress was achieved on the AD front (see below), but agreement was reached to ban the use of VERs and to make Article XIX more attractive to import-competing industries. Progress on the latter front was facilitated because importing country governments increasingly recognized that VERs were costly and not very effective—something that economists did not stop from pointing out in study after study (for example, De Melo and Tarr, 1992). Voluntary export restraints encouraged quality upgrading by affected exporters and entry by new exporters, including affected firms that relocated production facilities to other countries.

The Uruguay Round Agreement on Safeguards

A major achievement of the Uruguay Round Agreement on Safeguards was the prohibition of VERs and similar measures on the export or the import side (such as export moderation, export-price or import-price monitoring systems, export or import surveillance, compulsory import cartels and discretionary export or import licensing schemes). Any such measure in effect as of January 1995 was to be brought into conformity with the new rules or phased out by mid-1999.

The agreement requires that safeguard measures be taken only if an investigation demonstrates that imports have increased so much to have caused or threaten serious injury to an import-competing domestic industry. Investigations must include reasonable public notice to all interested parties and public hearings or other mechanisms through which traders and other affected parties can present

their views on whether a safeguard measure would be in the public interest. Investigating authorities must publish a report setting forth their findings and reasoning.

Serious injury is defined as a significant overall impairment in the situation of a domestic industry. In determining injury, the domestic industry is defined as those firms whose collective output constitutes a major share of total domestic output of the product concerned. Factors to determine whether increased imports have caused serious injury include the magnitude of the increase in imports, change in market share, and changes in the level of sales, production, productivity, capacity utilization, profits and employment of the domestic industry. The AB in its case law has made clear all mentioned factors must be examined. A causal link needs to be made between increased imports and serious injury or threat thereof. Imports do not have to be the sole or even the major source of injury, but if factors other than increased imports are also causing injury to the domestic industry, such injury may not be attributed to increased imports.

Protection is limited to what is necessary to prevent or remedy serious injury caused by imports. If a QR is used, it may not reduce imports below the average level of the last three representative years, unless clear justification is given that a lower level is necessary to prevent or remedy serious injury. Although in principle safeguard actions must be nondiscriminatory, QRs may be allocated on a selective basis if the Committee on Safeguards accepts that imports from certain members have increased disproportionately in comparison to the total increase in imports, and the measures imposed are equitable to all suppliers of the product. Such 'quota modulation' may be maintained for four years at the most.

If use is made of QRs, they may be administered by exporters if this is mutually agreed. Thus, although VERs are prohibited, something analogous may be used if implemented as part of a GATT-conform procedure. Safeguard actions based on absolute increases in imports that are consistent with the provisions of the agreement do not require compensation of affected exporting countries for the first three years. In principle, safeguard instruments should be degressive—the level of protection should decline over time—and not last more than four years. All actions are subject to a sunset clause. The maximum total number of years a safeguard may be applied is eight years. If an action is extended beyond four years, a necessary condition is that the industry demonstrates that it is adjusting. If individual market shares of developing countries are less than 3 per cent of total imports, and the aggregate share of such countries less than 9 per cent of total imports, they are exempt from safeguard actions.

Notwithstanding the many procedural requirements, if governments want to they can put in place provisional safeguards virtually immediately. Article XIX is not called 'Emergency Action' for nothing—in 'critical circumstances' the Agreement on Safeguards allows Members to put in place safeguards immediately on a provisional basis (Article 6). As put by Vermulst, Pernaute and Lucenti (2004),

'...the safeguards instrument is an extraordinarily blunt instrument capable of very rapid deployment against imports covering broad categories' (p. 26).

Summing up, the Agreement of Safeguards brought existing practices that were GATT-inconsistent inside the tent, but subjected their use to multilateral surveillance and rules. Thus, VER-type measures came to be permitted under the WTO in certain conditions—in contrast to GATT 1947. Although this implies a move away from economically superior policies in an abstract sense, this is the price that had to be paid to avoid continued circumvention of GATT 1947 disciplines, which had become increasingly irrelevant. In addition, although the new agreement maintained the requirement that governments taking an action should enter into compensation discussions with affected exporters, the latter were not permitted to retaliate during the first three years of a safeguard. This example of creative drafting aimed at making the use of safeguards easier.

The WTO experience with safeguards

In the first 12 years of the WTO, members initiated 118 safeguard investigations, implying an annual average rate that was more than double what had prevailed in the GATT years (Table 9.2). This suggests that the intended weakening of WTO rules had the desired effect, especially as much of the increase reflects greater invocation of the instrument by developing countries—i.e. new users. Although the deal seems to have stuck in the sense that VERs are no longer prevalent, compared with other instruments of contingent protection such as antidumping (see below) safeguard measures continue to be used relatively infrequently.

Reasons for this probably include not only the continued relatively easier access to AD, but also the legal uncertainty that surrounds the use of safeguards. The WTO case law has not been kind to countries using safeguards—every case that has been contested has been lost by the safeguard-invoking country. Indeed, among the three major instruments of contingent protection, use of safeguards has been contested by far the most frequently relative to the total number of times the instrument has been used by WTO members. This is because key terms such as 'unforeseen developments', 'serious injury', 'increased quantities' and 'cause' are

Table 9.2. Safeguard measures (1995–2007)

	1995–9	2000–3	2004–7	Total
OECD countries	8	20	2	28
Developing countries	8	25	22	55
Total	16	45	24	83

Note: Annual data span 1 November to 31 October.

Source: WTO, Safeguards Committee Annual Reports; WTO Annual Reports.

not defined in the agreement. Without clarity regarding the baseline to be applied to imports, how to assess the link between imports and injury, and what constitutes an 'unforeseeable' event that generates an import surge, governments confront great uncertainty on whether the approaches they follow will pass muster.

Sykes (2003) and Grossman and Sykes (2007) argue in some detail that the AB has not done much to clarify matters. Instead it has simply reverted to the language of Article XIX and the Agreement on Safeguards in reviewing panel decisions, without clarifying the meaning of the key terms. Particularly problematical has been the insistence of the AB on applying the 'unforeseen developments' test to safeguard actions. In practice this had ceased to be applied or considered relevant by GATT contracting parties, and for that reason is not included in the Agreement on Safeguards. The re-introduction of this test by the AB effectively reversed the intent of those who had negotiated the Safeguards Agreement. Overall, 'Appellate Body decisions since the inception of the WTO have only made matters worse, to the point that the legal requirements for the use of safeguards are largely incoherent, and no nation can employ them without the near certainty of defeat in the dispute resolution process should they be challenged' (Grossman and Sykes, 2007: 91). Sykes (2003) concludes that the incoherence can only be resolved through a re-negotiation of the agreement or through action by the AB to define key terms. To date it has not been willing or able to do so.

Given the length of the WTO dispute settlement process—some three years on average—in effect WTO members have three years to impose a measure that violates tariff bindings. Perhaps not coincidentally, this is the same period provided under the Safeguard Agreement during which no retaliation may be implemented by affected exporters. The lack of clarity regarding the rules of the game increases the incentives for governments to take actions they deem necessary and wait for dispute settlement to take its course.

Although the absolute number of safeguards has been relatively small, it is important to take into account that safeguards, if they conform to WTO rules, will be nondiscriminatory and thus affect *all* imports. This is not the case with AD. Thus the economic impact of one safeguard can greatly exceed that of a number of AD actions. The 2002 US Steel Safeguard is an example of an action that had a major impact on trade—and that generated a series of disputes (Box 9.1).

Analysis of the impacts of post-Uruguay Round safeguard actions by Bown and McCulloch (2007) suggests that in practice these measures have often not conformed with the MFN principle, due in part to the *de minimis* provisions that are applied to exclude small developing countries from the reach of the measure. Another source of discrimination in the application of safeguards is that PTA partners are often excluded. Bown (2007) finds evidence that Canada's use of trade remedies was structured in a way so as to reinforce the discrimination that underpins the NAFTA.

Box 9.1. The 2001–2 US Steel Safeguards

The steel industry in the United States has a long history of being protected and subsidized. A variety of QRs were put in place starting in the 1970s, as well as hundreds of AD and CVD actions in the course of the 1980s and 1990s. The protection of the industry was costly given that steel is a key input into numerous sectors that together generate much more value added than does the steel industry itself. In 2001, steel users in the US employed 57 workers for every employee in steel (Ikenson, 2002). Moreover, parts of the industry were modern and competitive, in particular the so-called mini-mills that relied on scrap metal as feedstock.

In 2001, the industry sought additional protection once again, this time in the form of an across-the-board safeguard action. The US ended up imposing safeguard tariffs ranging between 8 and 30 per cent on ten steel product groups (a total of 272 ten-digit tariff lines). Steel imports from PTA partners (Canada, Israel, Jordan and Mexico) were excluded from these measures, as were imports from 100 developing countries that fell under the *de minimis* provision. There were also firm-specific 'product exclusions'. These were driven by the needs of steel-using firms, which had been asked by USTR to submit requests for exclusions of products that were critical to their production and that could not be supplied by US firms. The United States Trade Representative granted about 1,000 firm-specific exemptions, permitting continued imports from specified foreign steel-producing firms. (The exclusions were *not* for the specific products concerned—i.e. they were not MFN exclusions, but applied only to specified suppliers.)

The result of these various exemptions was that affected exporters confronted an effective tariff increase that was higher than would have occurred if the safeguard had been truly MFN. Bown (2004*d*) estimated that overall imports of the affected steel products fell by some 14 per cent in the year following the increase in tariffs; but exports of the nonexempted suppliers dropped by some 30 per cent (or US$1.2 billion). He concludes that the country and product exclusions resulted in an outcome that was akin to what would have been observed if the US had imposed a series of AD and CVD actions—as it had in fact done in the 1990s. The US action illustrated how a safeguard action can be manipulated to provide the same sort of discriminatory treatment as the explicitly discriminatory AD law.

In 2002, nine WTO members—Brazil, China, Chinese Taipei, the EU, Japan, Korea, New Zealand, Norway and Switzerland—challenged the safeguard action in the WTO. The panel found that the safeguards violated Articles 2.1, 4.2(b) and 3.1 of the Agreement of Safeguards by failing to show a 'causal link' between increased imports and serious injury and by failing the 'parallelism' requirement. The latter calls for a country taking an action to base the duties imposed on the injury caused by the countries included in the injury investigation (the US was found not to have done what was needed to exclude the effect of imports from its PTA partners in determining the cause and level of injury). Moreover, the US failed to provide a reasoned and adequate explanation demonstrating the impact of the 'unforeseen developments' it had identified on imports and how the facts supported the US determination of an increase in imports.

The unforeseen developments identified by the US included the Asian financial crisis and the collapse of the Soviet Union, both of which were argued to have led to a collapse in demand, with the resulting excess production of steel directed at the US market.

(*cont.*)

Box 9.1. (*Continued*)

Although the panel was sympathetic towards this argument the problem for the US was that US law makes no reference to the 'unforeseen developments' test and that it had not been applied in the investigation as a cause of increased imports.

On appeal, the panel's findings were substantially up-held for all products concerned. Given noncompliance by the US, the EU was authorized to raise tariffs amounting to US$2.2 billion on US goods. It targeted products such as citrus fruit and textiles in an effort to mobilize internal political opposition to the US measures in question. The US responded in December 2003 by terminating the safeguard measures.

This safeguard action had several spillover effects. One was that the EU immediately responded to the US action by launching 21 safeguard actions of its own for the steel products concerned—imposing provisional tariff quotas the very same day the US measures were announced for 15 categories of steel products. This was driven by a fear of trade deflection—the EU sought to foreclose its market to the exporters most affected by the US action. The EU motivated its measures as a response to the 'unforeseen' US action. The European measures were removed in December 2003, in parallel with the termination of the safeguard by the US.

Bown and Crowley (2007) present indirect evidence that the EU fears may have been justified. They analyze the impact of US safeguards on Japanese exports. They find that US action led to a decline of 60–70 per cent in the value of Japan's *overall* exports of affected products—in part because excess supply created by the safeguard in other markets prevented Japanese exporters from diverting output elsewhere.

Source: Bown (2004*d*); Vermulst, Pernaute and Lucenti (2004); Grossman and Sykes (2007).

Special safeguards: Textiles and Clothing, Agriculture and Accession Protocols

Special safeguard actions have been included in some WTO agreements, in particular the WTO Agreements on Textiles and Clothing (ATC) and the Agreement on Agriculture, which has a Special Safeguard (SSG) clause. Both of these are discussed in Chapter 6. Special provisions allowing for country-specific safeguards were also included in China's Protocol of Accession—see Chapter 12. Historically, the GATT nonapplication clause was sometimes used in lieu of the type of specific provisions written into China's accession protocol. The best known example occurred in the case of Japan's accession. At the time there was strong pressure from some contracting parties to introduce a new Japan-specific safeguard mechanism. This was rejected, and led to over a dozen contracting parties invoking Article XXXV ('Non-Application of the Agreement between Specific Contracting Parties') when Japan acceded. In a number of cases, Japan subsequently negotiated bilateral agreements containing special safeguard clauses that led to revocation of Article XXXV.