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Developing countries emphasize development, LDC issues in WTO talks

Several developing countries have called for high priority to be accorded to issues touching on least developed countries' (LDCs) interests, and for the development dimension to be at the centre of the work programme for concluding the Doha Round trade talks. These countries put forward their views at a 20 February meeting of the WTO General Council, which also heard the WTO Director-General's assessment of the Doha Round as experiencing slow progress but moving forward.

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South stress on development, LDC issues in post-Bali work

Developing countries have highlighted the need to tackle issues relating to the least developed countries and the importance of advancing development objectives in the Doha Round trade talks at the WTO.

by Kanaga Raja

GENEVA: The meeting of the WTO General Council on 20 February heard a number of developing countries calling for high priority to be accorded to the least developed countries' (LDCs) issues, and for the development dimension to be at the centre of the post-Bali work programme for concluding the Doha Round.

The developing countries also stressed that the Rev.4 draft agriculture modalities text and the Rev.3 draft NAMA modalities text should be the basis for the negotiations. They further called for a transparent, inclusive and bottom-up approach in the negotiations on defining the work programme.

Progress report

At the meeting, WTO Director-General Roberto Azevedo, as Chair of the Trade Negotiations Committee (TNC), had provided an overview of the progress to date on each of the Doha Round negotiating areas including agriculture, non-agricultural market access (NAMA), services, rules, TRIPS issues, trade and environment, trade and development, and the Dispute Settlement Understanding (DSU) negotiations.

On agriculture, he reported that the focus in the consultations so far had been mostly on the domestic support and market access pillars. He said it was clear that all elements within the agriculture framework were inter-related and there seemed to be a general acceptance that they would need to be dealt with as an overall package.

Azevedo said there had been a good level of attendance and engagement at these consultations and the chair of the agriculture negotiations would be continuing his consultations and convene an informal meeting of the Special Session of the Agriculture Committee in the near future.

In the Negotiating Group on Market Access, the main focus of the chair's consultations had been on tariffs, and these consultations had shown that work should mainly focus on the so-called "formula-applying members" in a first stage.

Certain ideas had been orally presented in terms of an alternative approach to the Swiss formula in the Rev.3 draft NAMA modalities text, said Azevedo. At this stage these were only ideas which would need, at some point in time, to be translated into more concrete proposals.

An open-ended meeting of the Negotiating Group had been scheduled for 2 March to discuss the observations from these consultations and for information-sharing on activities amongst members in respect of non-tariff barriers, said Azevedo.

On services, Azevedo reported that over the past few weeks the chair of the services negotiations had consulted over 40 delegations, in a variety of configurations, on the next step in the services component of the work programme.

On the issue of trade and development, Azevedo said that proponents had tabled two lists of S&D (special and differential treatment) provisions that they would like to be taken up as part of the work programme. Although the negotiations awaited concrete textual proposals by the proponents soon, Azevedo said that this marked a forward step in an important area of work.

On the DSU negotiations, Azevedo said that the work had led to the presentation of "conceptual elements" of possible solutions in all 12 issues under discussion. These elements did not, at this stage, reflect full convergence. Nor did all participants perceive these elements, taken together, as necessarily reflecting an adequate overall balance of interests.

Azevedo was of the view that members had had a productive start to the intensive process that was launched in January, and in the past few weeks, they had started to engage more substantively, particularly in the three core areas (i.e., agriculture, NAMA and services).

"Progress is slow, but we are moving forward," said the Director-General.

Substantive positions had not changed a great deal since the last time these issues were discussed, but the tone of the discussions was more positive.

To find solutions members needed to move away from general statements of what they hope is desirable, and also away from finger pointing, to a situation where they identify more clearly the problems and challenges ahead of them, and explore potential solutions for each of those problems and challenges.

He said he was not suggesting that members move away from the existing mandates or guiding principles. "I am simply suggesting that we have to explore alternative approaches and alternative paths which fit within them."

Noting that the conversation would be deepened over the next two or three weeks under the negotiating group chairs' process, Azevedo said the key word was "doability", meaning what was doable for all members and not just for some.

Azevedo urged members to talk directly to each other, and stressed the need to get into a solution-finding mode.

Strong support

A number of delegations spoke following the Director-General's report. According to trade officials, Saudi Arabia, on behalf of the Arab Group, indicated its strong support for the multilateral trading system and the Doha Development Agenda (DDA). The deadlines for the implementation of the Bali decisions must be respected, it said.

It said that recently acceded members (RAMs) should have additional flexibilities. Many of these countries had undertaken extensive commitments as part of their accession process and this needed to be recognized.

Saudi Arabia also stressed that the development dimension must be the overarching principle.

Burkina Faso, on behalf of the Cotton-4 grouping, said it was essential that the resolution of the cotton issue be a part of the Bali work programme, and that there be deliverables by the 31 July deadline (for drawing up the work programme for concluding the Doha Round).

It appealed to all stakeholders to give high priority to cotton to ensure appropriate answers to the problems being faced by West African cotton growers.

It would also like to have an agreement in all areas by the 10th WTO Ministerial Conference (MC10, to be held in Nairobi from 15-18 December this year).

Chinese Taipei, on behalf of the RAMs, said that agriculture, NAMA and services were at the centre of these negotiations. They needed to be tackled in parallel and sequencing (of these issues) was not an option.

The post-Bali work programme should be something doable, and the level of ambition must be something affordable for all members. Having said this, it stressed that the level of ambition must be more than nothing.

Referring to comments from members that the Rev.4 agriculture and Rev.3 NAMA texts were the preferred starting point for the negotiations, it noted that it had heard from some members that they would like to have new proposals considered.

It urged these members to translate ideas such as request-and-offer approach, average tariff cuts and tariff simplification into concrete proposals as soon as possible so that there could be real traction in terms of the negotiations and engagement.

The flexibilities accorded to developing countries, the LDCs and the RAMs that were contained in the texts needed to be taken into account, it said.

The RAMs had already made deep concessions which should be taken account of, it said, adding that there was a need to adhere to the mandates of the Doha Ministerial Declaration, the Hong Kong Ministerial Declaration and the July framework.

Other countries should at the minimum be prepared to do as much as the RAMs had done as part of their accession process. The percentage of tariff lines that were duty-free in the RAMs was higher than the WTO average and the percentage of tariff lines that were tariff peaks was lower. Members should see this as an example.

Brazil said that it would like to see considerable levels of ambition in all three pillars of the agriculture negotiations – export competition, domestic support and market access – as well as in cotton.

"Connecting the dots"

The United States said that in its view, the past few weeks had been a relatively productive period in the development of a post-Bali work programme for the Doha Development Agenda.

"We have been in a necessary process of 'connecting the dots' in the current landscape of the DDA and dealing honestly and directly with the picture that is revealed. When we connect the dots, what is revealed, undeniably, is that we are nowhere near consensus. We are quite distant from a common view of what a work programme should look like, or how it could realistically enable us to conclude the Round in a manner that works for everyone, and that can be accomplished in a relatively rapid timeframe."

The US claimed there were now clear indications from a number of members, both developed and developing, that the Rev.3 text in NAMA was not a viable basis for concluding the negotiations, while others remained attached to that text.

Another example, in the US view, was the very stark presentation of facts regarding Rev.4 (agriculture text), demonstrating that only one member – namely, the US – would be required to cut into current domestic support programmes, while members whose programmes had grown exponentially since 2008 would make no meaningful contribution.

"Meanwhile, those members have stated clearly their expectation that this mind-boggling imbalance, which would clearly fall short of any true effort to reform trade-distorting agricultural subsidies, should be preserved. Using the lexicon of the WTO, we view that as blood for water – or blood for air – which is simply not an outcome that we could endorse."

In the US' view, "we must continue to recalibrate. We are collectively better positioned than we were a few weeks ago to really start tackling the question of what recalibration means."

The US noted that during one of the recent informal meetings in Room W (at the WTO), there was a refreshingly direct exchange on the concept of "differentiation" in the roles and contributions of developing-country members.

The US said it wanted to be clear about what it did and did not mean when it referred to differentiation. "We do not mean that we are seeking a new categorization of members within the WTO. We are not talking about 'graduation'. We recognize such a discussion would result in endless debate and no outcome, and furthermore it is not what we need in order to accomplish a reasonable outcome."

What the US meant was that, for example, "a developing country member that today maintains very signifi-

cant agricultural domestic support programmes and has the productive capacity to affect global markets will necessarily have to participate in negotiations, and contribute to outcomes, in ways that are different than developing countries that don't have such programmes."

According to the US, such developing countries "are different from other developing countries, and we cannot succeed if we pretend otherwise. But let me also be clear: the United States is not seeking new market access outcomes in Doha from those WTO members who would not have applied the formula under the existing NAMA framework."

"We are simply trying to prompt an honest discussion of world trade as it exists today and to foster an outcome that reflects real world trade dynamics. None of this requires any revision of categories within this institution, but it does implicate the need for a flexible approach that recognizes that there can be no one-size-fits-all approach for development," said the US.

Crucial year

Bangladesh, on behalf of the LDCs, said that this was a crucial year for the WTO, and highlighted the need to get an agreement on the post-Bali work programme by the end of July.

On the LDC-specific issues, it noted that there had been a meeting held on rules of origin and a high-level meeting on the LDC services waiver. There had been good progress but much work needed to be done, it said.

It cited a recent report by the UN Conference on Trade and Development (UNCTAD) which pointed out that the current account deficits of the LDCs were widening to $40 billion, and added that this was likely to widen further on account of falling commodity prices.

It was very important that the issues of importance to the LDCs be concluded by 31 July, it said.

On the services waiver for the LDCs, it would like to see those countries that had made pledges at the high-level meeting on 5 February make notifications locking in those pledges by the deadline of 31 July.

It did not want to see coming out of any post-Bali work programme a situation that would land the LDCs in a worse position than other non-LDC members. It would also like to see positive decisions on duty-free, quota-free market access for LDC products.

Lesotho, on behalf of the African Group, endorsed the LDC and Cotton-4 statements. It was encouraged by what it had seen with respect to more focused and specific discussion particularly on agriculture. It was of the view that the Rev.4 draft agriculture modalities text was a good starting point.

Trade-distorting domestic support in agriculture was an issue for the African Group, it said, adding that it would like to see good disciplines in terms of overall trade-distorting domestic support levels as well as product-specific caps.

Barbados, on behalf of the African, Caribbean and Pacific (ACP) Group, said it wanted a good outcome on the post-Bali work programme by the stipulated deadline, with the concept of the development dimension being preserved and at the front and centre.

It would also like to see the issues of importance to LDCs addressed, and the Rev.4 agriculture text and the Rev.3 NAMA text reflected in any outcome. The issue of longstanding preference erosion and the LDC issues were of crucial importance to the Group, it said.

Guatemala, on behalf of the grouping of small and vulnerable economies (SVEs), stressed the importance of a transparent, inclusive and bottom-up process. The important principles that

TRIPS amendment, Jones Act also discussed at General Council

At the 20 February WTO General Council meeting, Director-General Roberto Azevedo also made a statement under the agenda item of Protocol Amending the TRIPS Agreement.

WTO members had agreed in December 2005 to amend the WTO's Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) to secure a permanent solution for the problem identified in Paragraph 6 of the Doha Declaration on the TRIPS Agreement and Public Health. This problem concerned the difficulties that WTO members with insufficient or no manufacturing capacities in the pharmaceutical sector could face in making effective use of compulsory licensing under the TRIPS Agreement.

Members took a decision to solve this problem by giving permanent legal effect, and not just a waiver, to a new kind of compulsory licence – a special compulsory licence for export, Azevedo said.

It had been 10 years since that agreement was reached. And "we are still to bring that agreement into force", the Director-General said, adding that it was high time to finalize this process.

"The 2005 decision was a clear recognition by all WTO members of the importance of providing a permanent legal certainty to this new compulsory licensing system under the TRIPS Agreement"; currently access to medicines through compulsory licensing can take place on the basis of a waiver.

Noting that two-thirds of the membership have to confirm acceptance before the amendment comes into force, Azevedo said that 27 more acceptances were needed.

He had written to ministers of all relevant countries who had not yet taken this step to urge them to formally accept the TRIPS amendment.

"It's time that we completed this process and that the amendment is brought into force," he said.

The General Council on 20 February also took up the agenda item of review of the exemption provided under paragraph 3 of the General Agreement on Tariffs and Trade (GATT) 1994.

This is a waiver that has been in place since 1994 relating to the US Jones Act – Merchant Marine Act of 1920 – which requires all transport of goods by water between US ports to be carried out in vessels that have been constructed in the US itself.

According to trade officials, several delegations including Japan, Korea, China, Chinese Taipei, Hong Kong-China, Canada, Norway, the EU and Australia voiced criticism of this particular provision, insisting that the US explain very clearly why there is a need for continuing with this exemption from GATT/WTO principles.

According to trade officials, the US said that it had provided statistical information on the number of vessels that had been built.

This was a critical part of the Uruguay Round Agreements, the US said, adding that the shipbuilding capacity of its shipyards was essential for the US to maintain its navy for defence purposes. *– Kanaga Raja (SUNS7968)* ❐

had been highlighted in the various Ministerial declarations must be preserved, it said. It was also important that in the discussions, the flexibilities that had been obtained by the SVEs in the draft texts be recognized.

The European Union said that the success of the Bali Ministerial Conference had given the WTO another opportunity, perhaps its last, to come to a successful conclusion of the DDA, and "it is our fundamental and collective responsibility not to miss this opportunity."

In this context, the EU said, "we need to maintain the focus of our efforts on exploring what can be done and achieved today, and not on what we would have liked to get 14 years ago at the time of the Round's launch, or 7 years ago when we were so close to a deal."

The EU said it was ready to continue to look to creative solutions in all areas, as long as everyone else was willing to do the same. All of the core issues needed to be taken forward in parallel and would have to achieve commensurate levels of ambition.

Still, the EU accepted that agriculture may determine what will and won't be possible in the DDA overall, keeping in mind, however, that finally a balance would be needed within the agriculture pillar as between all the areas of a possible outcome.

On the next steps, the EU agreed with the Director-General that it was crucial at this stage that the necessary technical work be taken forward.

The market access pillar – in both agriculture and NAMA – was a particular case in point. The need for a simpler, more realistic market access approach had been stressed by a large number of members during the conversations up until now, it said.

Useful work on non-core issues like rules and TRIPS could also move forward aiming at exploring what elements could realistically be part first of the work programme and then of a possible DDA outcome, it added.

According to the EU, the first weeks of this year had shown that slowly but surely members were beginning to open up to the idea and to converge towards the need of exploring possible realistic solutions in all areas. "This is the mindset that we need in order to advance and to keep our July work programme deadline as well as to see concrete results by MC10."

Ambitious and detailed

According to trade officials, China associated itself with the statement by the RAMs. There was a need to sow seeds now so that members could achieve an ambitious and detailed post-Bali work programme by 31 July and have a result by MC10. There was also a need for adherence to the Doha and Hong Kong Ministerial mandates, as well as the Bali mandate and the 2004 framework.

On the issue of domestic support in agriculture, China said that it was very important not to mix up different kinds of domestic support. There were different natures and different purposes as well as different histories and different per capita sizes with respect to domestic support programmes, it said. There were programmes that supported big rich farmers for commercial purposes and there were those that supported the livelihoods of hundreds of millions of small poor farmers.

Members must build on the work of the Rev.4 agriculture text and the Rev.3 NAMA text, said China.

While there was a need for recalibration, members' comfort levels should be taken care of in terms of dealing with any recalibration. There should not be any scenarios in which only a few members suffer discomfort.

China also stressed on the need for a transparent and inclusive approach. It said that recalibration should be non-discriminatory, and if there was a readjustment for some, it must apply to all.

China pointed out that the Doha Development Agenda was a development round. Special and differential treatment and the principle of less than full reciprocity and flexibilities for the LDCs must be preserved.

Cuba stressed on a transparent and inclusive process. The post-Bali work programme must include all of the Doha issues and have priority for the developing countries. There could be recalibration but the mandate should not be reinterpreted, it said. It endorsed the development dimension mandate, saying that this must be preserved. The flexibilities that applied to some countries – and even to specific countries – must also be preserved, it said.

Intensive engagement

India said that an intensive process of engagement had begun, and that members were in the process of developing a clearly defined post-Bali work programme.

There was a need to seek the right level of ambition starting with agriculture, it said, adding that the existing mandate had to be respected, as well as the progress that had already been achieved.

Equitable, balanced and development-oriented outcomes must be sought through a transparent and inclusive process, it said. Trade for development was the objective of this round; it was not a round designed to enhance market access.

The global trading system was highly inequitable and trade did not necessarily lead to development, it said.

It stressed the importance of policy space. Trade for commercial purposes that impinges on policy space could not deliver development, it said, underlining the need to level the playing field.

Japan expressed frustration over the slow progress being made, saying that some countries were simply repeating their basic positions going back a long time.

Paraguay said that members were having frank discussions but did not have a clear idea of what they were seeking. It said that export competition needed to be tackled, as did trade distortions in cotton. *(SUNS7968/7970)* ❐

LDCs request extension of transition period on pharmaceuticals

Pointing to the "massive health challenges" they face, the least developed countries have sought continued exemption from subjecting pharmaceutical products to the intellectual property rules imposed by the WTO.

by K.M. Gopakumar

NEW DELHI: The least developed countries (LDCs) have submitted a request for the extension of the transition period with regard to intellectual property protection of pharmaceutical products.

The request seeks an extension from 1 January 2016 to as long as the World Trade Organization member remains a least developed country.

The transition period exempts LDCs

from most obligations under the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS).

The current transition period on pharmaceutical products, granted in 2002 in pursuant to Paragraph 7 of the Doha Declaration on the TRIPS Agreement and Public Health, will end on 1 January 2016.

The formal request was submitted on 20 February by Bangladesh on behalf of the LDC Group and posted officially by the WTO secretariat on 23 February. It was introduced at the WTO's TRIPS Council on 24 February and a brief discussion continued the following day.

The request is expected to kickstart a series of negotiations this year for the extension of the transition period.

[Under Article 65.1 of the TRIPS Agreement, the LDCs obtained a 10-year transition period for the implementation of the Agreement including on product patent protection of pharmaceutical inventions. In 2001, trade ministers, through the Doha Declaration on the TRIPS Agreement and Public Health, instructed the TRIPS Council to extend the transition period related to pharmaceutical products up to 1 January 2016.

[This extension was done without prejudice to the possibility of further extension of the transition period with regard to the implementation of the TRIPS Agreement (general exemption) under Article 66.1 wherein the TRIPS Council "shall, upon duly motivated request by a least developed country Member, accord extensions of this period". Under this provision LDCs obtained two extensions of the transition period with regard to the implementation of the TRIPS Agreement – in 2005 to 2013, and in 2013 to 2021. Thus, the extension of the transitional period on pharmaceutical products is additional to the general exemption granted in 2013 and expected to go beyond 2021.]

"Weakest and most vulnerable group"

At the TRIPS Council meeting on 24 February, Bangladesh made an impassioned statement on behalf of the LDC Group on the request for extension regarding pharmaceutical products. Several developing countries subsequently took the floor to support the LDC request.

Bangladesh said that the "LDCs represent the weakest and most vulnerable group of the community of nations. With deficiency and hardship touching all aspects of life, the population have been suffering from, and are highly susceptible to different forms of diseases. As a result, there are many other associated risks and impediments such as access to medicine and health services".

Bangladesh stressed: "Though we have a general TRIPS waiver up to 2021, considering the gravity of the situation of lack of access to medicine and proper health care, LDCs require time to reasonably overcome their public health problem."

Key parts of the request were highlighted in the statement (see below for details).

If the current request is approved, the LDCs need not implement product patent protection in relation to pharmaceutical inventions even beyond the current 2021 timeline for the implementation of the TRIPS Agreement, as the pharmaceutical exemption is sought for a member that remains an LDC.

The request for the extension of the transition period also covers test data protection under Article 30.3 of the TRIPS Agreement. It also seeks exemption from the "mailbox" (Article 70.8) and exclusive marketing rights (Article 70.9) provisions of the Agreement.

(Under Article 70.8, during the transition period on pharmaceutical patents a WTO member is to receive patent applications and examine those applications and apply to these applications, as of the date of application of the Agreement, the criteria for patentability as laid down in the Agreement as if those criteria were being applied on the date of filing in that member or, where priority is available and claimed, the priority date of the application. The duration of the patent would be counted from the date of filing.

(Under Article 70.9, a WTO member which is availing of the transition period with regard to patent protection of pharmaceutical patents shall give exclusive marketing rights for a period of five years after marketing approval is obtained in that member or until a product patent is granted or rejected in that member, whichever period is shorter, provided that, subsequent to the entry into force of the WTO Agreement, a patent application has been filed and a patent granted for that product in another member and marketing approval obtained in such other member.)

The LDC request clearly spells out the need for the extension of the transition period in light of the current health situation of LDCs.

It states: "In 2011, some 9.7 million of the 34 million people living with HIV worldwide, live in LDCs. Of the people living with HIV in LDCs, 4.6 million were eligible for antiretroviral (ARV) treatment in accordance with the 2010 World Health Organization HIV treatment guidelines, however, only 2.5 million were receiving it. While the ARV treatment situation may have somewhat improved since the 2001 Declaration on TRIPS and Public Health … the need remains significantly great. There are particularly complex challenges for LDCs with respect to second line HIV treatment which is more than double the price of the first line regime, and third line HIV treatment which could be as much as 15 times the price of first line treatment."

The request cites concerns expressed by the Joint United Nations Programme on HIV/AIDS (UNAIDS) that "without extension of the transition period, access to antiretroviral therapy and other key medicines in LDCs will face real challenges" and "a real danger ... progress that has been made to improve access to HIV-related medicines in these countries will be reversed".

It also cites cancer incidence in LDCs, "which is expected to rise 82% from 2008 to 2030 in low-income countries (compared to 58% in upper-middle and 40% in high-income countries)".

Reference is also made to a June 2013 resolution adopted by the UN Human Rights Council which urges states to promote access to medicines for all, including through the use, to the full, of the provisions of the TRIPS Agreement which provide flexibility for that purpose.

The request further notes that the original extension of the transition period on pharmaceutical products "has facilitated access to affordable medicines in LDCs. However, LDC members of the WTO continue to face massive health challenges from communicable and non-communicable diseases".

In addition, the request also seeks extension on other grounds contained in Article 66 such as lack of technological base and local manufacturing ability as well as the special needs of LDCs.

The request states: "In addition to the socio-economic and financial con-

straints, LDCs also lack adequate technological base and local pharmaceutical manufacturing capacity. These special needs and circumstances of LDCs, and the vulnerability of LDCs confirm the need for a renewed transition period for as long as these constraints remain."

Crucial

Health experts point out that the extension of the transition period is crucial for LDCs irrespective of the general exemption granted until 2021, rejecting the view that the general exemption is enough to take care of health needs.

According to these experts, the extension of the transition period on pharmaceutical products is unconditional and allows LDCs to suspend any TRIPS provisions related to pharmaceutical products. In contrast, the general exemption granted in 2013 has certain conditions that may be subject to interpretation and may be used against full suspension of existing provisions in some of the LDC intellectual property laws, which already provide some protection to pharmaceuticals.

(The 2013 general exemption extension states: "Recognizing the progress that least developed country Members have already made towards implementing the TRIPS Agreement, including in accordance with paragraph 5 of IP/C/40, least developed country Members express their determination to preserve and continue the progress towards implementation of the TRIPS Agreement. Nothing in this decision shall prevent least developed country Members from making full use of the flexibilities provided by the Agreement to address their needs, including to create a sound and viable technological base and to overcome their capacity constraints supported by, among other steps, implementation of Article 66.2 by developed country Members.")

The LDC request is expected to be discussed at length in an upcoming meeting of the TRIPS Council in June.

A delegate from the Indian mission participating in the February TRIPS Council meeting informed the Third World Network that "India supports all initiatives to promote access to medicines at affordable cost in poor countries".

Meanwhile, the request has been widely welcomed by health experts and activists.

The international medical humanitarian organization Medecins Sans Frontieres (MSF) welcomed the request to extend the pharmaceutical transition period until LDCs are no longer classified as such. Referring to their work in many LDCs and their reliance on low-cost generic medicines to provide affordable access to treatment, Rohit Malpani, Director of Policy and Analysis of the MSF Access Campaign, said: "Any flexibility which can safeguard access to low-cost generic medicines and vaccines is welcomed by MSF." *(SUNS7970)* ❒

No common ground on NAMA, says chair

The chairperson of the WTO negotiations on liberalizing trade in manufactured goods has bemoaned the lack of headway in the talks.

by Kanaga Raja

GENEVA: The chair of the WTO Negotiating Group on Market Access for Non-Agricultural Products (NAMA), at an informal meeting on 2 March, urged members to come up with new ideas and proposals in order to find common ground, which does not exist at the moment.

According to trade officials, the NAMA chair, Ambassador Remigi Winzap of Switzerland, had convened the meeting following several consultations that he had held on the elaboration of the post-Bali work programme (which also includes the NAMA issues).

The chair gave the floor to members to voice their views, following which he concluded that "what's today on the table, as it stands, cannot fly".

Winzap said that he had heard some new ideas but there were no concrete proposals. The chair encouraged the members to come up with new ideas and to make proposals, either individually or in groups, in order to find common ground.

According to trade officials, Argentina proposed that the negotiations be conducted on a "request and offer" basis, encompassing the three main areas of agriculture, NAMA and services. This approach would involve no quantitative goals, no reduction formulae, no flexibilities and no requirement to engage. It will be implemented in a bilateral or plurilateral format and be demand-driven, with the least developed countries (LDCs) participating only if they are willing to.

Argentina said that it will present its proposal in the next few days. According to trade officials, Argentina said that it is ready to hear members' reactions on how issues such as the principle of "less than full reciprocity" (LTFR) in tariff reduction commitments, special and differential treatment, and preference erosion can be dealt with in the new proposal.

While a number of countries welcomed new ideas and initiatives, some voiced doubts about Argentina's proposal.

According to trade officials, the European Union said that the request-and-offer proposal has value but it "might not bring us closer to the result we expect", while Canada expressed some concerns.

Australia said that it does not think that it would be enough to achieve the desired result, while Brazil also expressed some doubts.

The US said that it was looking forward to seeing the proposal, while India said that it would assess it.

According to trade officials, other members including Thailand, Switzerland and Mexico said that the request-and-offer approach could be a good complement to the formula on cutting tariffs.

South Africa, Paraguay and Venezuela supported the proposal, trade officials added.

According to trade officials, many developing countries considered the Rev.3 draft NAMA modalities text to be a good basis for the negotiations, in particular due to the need to retain the flexibilities for developing countries that are contained in the text.

On the other hand, the EU, Canada, the US and, to a lesser extent, Korea did not consider the Rev.3 text to be a good basis to move forward.

According to trade officials, some members including Brazil, South Africa, Bolivia, Thailand and India reiterated that the level of ambition in agriculture would set the level of ambition in

NAMA.

According to trade officials, Argentina, Brazil, South Africa, Cuba and India stressed on the LTFR principle. Brazil said that the principle is non-negotiable, while India said that any reduction of tariffs should be based on the bound rates.

According to trade officials, Kenya, on behalf of the African, Caribbean and Pacific (ACP) group of countries, said that full account should be taken of the needs of developing countries. The negotiations on non-tariff barriers (NTBs) are critical for the group, it added.

Chinese Taipei said that the special situation of the recently acceded members (RAMs) should be fully taken into account.

According to trade officials, China said that the development component of the round should be paramount and that the flexibilities in the Rev.3 text should be preserved.

The Swiss formula for tariff reduction, as contained in the Rev.3 text, was favoured by some members including China, but rejected by others including South Africa.

The NAMA chair said that "most members are in general showing a certain openness to envisage alternative approaches to the Swiss formula".

On NTBs, many members consider them to be very important in the NAMA negotiations but said that the focus should now be on the contributions of the "formula applying members".

The chair said that he did not hear anything new in the discussion. He further said that the negotiations on NTBs without tariff negotiations are not possible.

The chair further concluded that NAMA cannot be seen in isolation since it is interdependent with all the other issues.

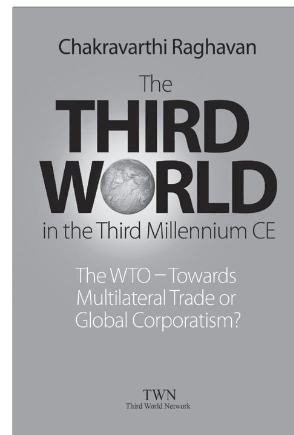
According to trade officials, Winzap said that the NAMA landing zones will be at a lower level than was envisaged in the Rev.3 text. He said that the Rev.3 text is not obsolete but there are difficulties for some members. The negotiating group also has to address the question of the Swiss formula, which creates problems for some members, he added.

The chair said that the only possible result in this negotiation is one that gets everybody on board. According to trade officials, he encouraged members to bring forward new proposals to try to find common ground. *(SUNS7974)* ❐

The Third World in the Third Millennium CE

The WTO – Towards Multilateral Trade or Global Corporatism?

By Chakravarthi Raghavan



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THE second volume of *The Third World in the Third Millennium CE* looks at how the countries of the South have fared amidst the evolution of the multilateral trading system over the years. Even at the General Agreement on Tariffs and Trade (GATT) gave way to the World Trade Organization (WTO) as the institution governing international trade, this book reveals, the Third World nations have continued to see their developmental concerns sidelined in favour of the commercial interests of the industrial countries.

From the landmark Uruguay Round of talks which resulted in the WTO's establishment to the ongoing Doha Round and its tortuous progress, the scenario facing the developing countries on the multilateral trade front has been one of broken promises, onerous obligations and manipulative manoeuvrings. In such a context, the need is for the countries of the Third World to push back by working together to bring about a more equitable trade order. All this is painstakingly documented by *Chakravarthi Raghavan* in the articles collected in this volume, which capture the complex and contentious dynamics of the trading system as seen through the eyes of a leading international affairs commentator.

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A new wave of trade protection?

Two US Congressional bills on currency manipulation threaten a new wave of trade protection and may also derail trade agreements like the TPPA, writes *Martin Khor*.

Two bills introduced in the United States Congress in February could lead to a new kind of trade measure that in the short run may wreck the Trans-Pacific Partnership Agreement (TPPA) and in the longer run could cause havoc in the global trading system.

The sponsors of the bills aimed at preventing "currency manipulation" claim to have majority support among Republicans and Democrats in both the Senate and the House of Representatives. Thus, these bills are being taken seriously, even if the administration of US President Barack Obama is known to be against linking the currency manipulation issue to trade measures.

The Congress members and their intellectual backers claim that some governments are deliberately manipulating their currency values to make them artificially low so as to reduce the prices of their exports, enabling them to sell more to the world market. The manipulating countries' imports are also thereby made more expensive, thus discouraging goods from other countries, the Congress members allege. They cite studies which claim that the US has lost 5 million jobs in the last decade because foreign governments have manipulated their currencies.

The main target of the bills is China, which has long been blamed by Congress members and some economists as currency manipulators. But other countries that have been mentioned are Japan, Malaysia and Singapore, in the context of the TPPA.

In an opinion article, Senators Sherrod Brown and Jeff Sessions and Representatives Sandy Levin and Mo Brooks (who are among the bills' sponsors) argued that the United States' high trade deficits with China are caused by the Chinese government's action to devalue its own currency against the US dollar. "This puts American manufacturers at a serious disadvantage and makes it more difficult for American companies to compete against Chinese companies," they claimed.

Though China is prominently targeted, the legislation can affect any country deemed to be "currency manipulators." The trade actions that the Congress members propose include:

- Enabling the American government to treat currency manipulation like illegal government subsidies or dumping of products at low prices. American companies claiming to be affected by foreign countries manipulating their currencies can petition the administration, which can then impose countervailing duties to offset the impact of currency manipulation on a US industry.
- The US government should include provisions in its trade agreements, starting with the TPPA, that would deter its trading partners from manipulating their currencies. The currency bills' content may thus be injected into the TPPA.

TPPA link

The timing of the tabling of the bills seems to be linked to the TPPA, which is reported to be near conclusion. A ministerial meeting is scheduled for March to address outstanding issues.

Many TPPA countries are reluctant or unwilling to conclude the negotiations unless the US President is given "fast-track authority" through a Trade Promotion Authority (TPA) law, meaning that Congress would only be able to vote for or against the agreement but not amend it. But the Congress members sponsoring the currency bills are making the passing of the TPA conditional on the adoption of the currency manipulation legislation. They also want the TPPA to contain provisions punishing currency-manipulating countries by suspending their TPPA benefits such as the preferential lowered tariffs.

In media reports on the Congressional bills, Japan was the country most prominently fingered as a TPPA country that could be considered a currency manipulator. But others were also mentioned. "Currencies rise and fall for lots of reasons, but US Sen. Sherrod Brown, congressional colleagues and a number of American manufacturers charge that China, Japan, South Korea, Malaysia, and Singapore have used financial and central-government mechanisms to keep their currencies artificially low – and that this gives their factories an unfair pricing advantage and undercuts American competitors," said an article by Stephen Koff of Northeast Ohio Media Group.

An article by the Peterson Institute's Fred Bergsten, who has been advising some of the Congress members behind the bills, states that Malaysia and Singapore, "which are engaged in [TPPA] negotiations, have also intervened and piled up sizeable reserves relative to any historical norms."

He mentioned three criteria for identifying currency manipulators: excessive official foreign currency assets (more than 3 to 6 months of imports); acquisition of significant additional amounts of official foreign assets, implying substantial intervention, over a recent period, say six months; and a substantial current account surplus.

The Congressional bills rely on IMF guidelines on what constitutes currency manipulation. These include large-scale intervention in one direction in currency markets; excessive accumulation of foreign exchange reserves; restrictions on or incentives for transactions or capital flows for balance-of-payments purposes; encouragement of capital flows through monetary policy for balance-of-payments purposes; fundamental exchange rate misalignment; and long and sustained current account surpluses.

The proposed legislation aims to counter currency manipulation used as trade protection or promotion. Ironically, however, it may lead instead to a big new wave of trade protection.

Critics are likely to see the US law as self-serving, as the US will be able unilaterally to define and decide who is a currency manipulator, and then to use trade measures such as tariff hikes and suspension of trade benefits.

Many governments and analysts have accused the US itself of lowering its currency's value through policies such as quantitative easing and near-zero interest rates. In their view, the US has also engaged in currency wars and can be considered a manipulator. If the US can take trade action against those it perceives as manipulators, others can also take action against the US.

Some US Congress members have defended US monetary policy as having legitimate aims, even though one effect

(continued on page 12)

South increasingly vulnerable in unstable global financial system

Deeper linkages with the global financial system are exposing developing countries to a heightened threat of shocks.

by Yilmaz Akyuz

After a series of crises with severe economic and social consequences in the 1990s and early 2000s, emerging and developing economies have become even more closely integrated into what is widely recognized as an inherently unstable international financial system.

Both policies in these countries and a highly accommodating global financial environment have played a role.

Not only have their traditional cross-border linkages been deepened and external balance sheets expanded rapidly, but foreign presence in their domestic credit, bond, equity and property markets has also reached unprecedented levels.

New channels have thus emerged for the transmission of financial shocks from global boom-bust cycles. Almost all developing countries are now vulnerable, irrespective of their balance-of-payments, external debt, net foreign assets and international reserve positions, although these play an important role in the way such shocks could affect them.

Stability of domestic banking and asset markets is susceptible even in countries with strong external positions. Those heavily dependent on foreign capital are prone to liquidity and solvency crises as well as domestic financial turmoil.

The new practices adopted in recent years – including more flexible exchange rate regimes, accumulation of large stocks of international reserves or borrowing in local currency – would not provide much of a buffer against severe external shocks such as those that may result from the normalization of monetary policy in the United States.

And the multilateral system is still lacking adequate mechanisms for an orderly and equitable resolution of external financial instability and crises in developing economies.

This process of closer integration was greatly helped by highly favourable global financial conditions before 2008, thanks to the very same credit and spending bubbles that culminated in a severe crisis in the United States and Europe.

The crisis did not slow this process despite initial fears that it could lead to a retreat from globalization. Integration has even accelerated since then because of ultra-easy monetary policies pursued in advanced economies, notably in the United States, in response to the crisis.

New vulnerabilities

The surge in capital inflows that started in the early years of the new millennium, and continued with full force after a temporary blip due to the collapse in 2008 of the Lehman Brothers financial services firm, holds the key to the growing internationalization of finance in developing countries.

It has resulted in a rapid expansion of gross external assets and liabilities of developing economies. More importantly, the structure of their external balance sheets has undergone important changes, particularly on the liabilities side, bringing new vulnerabilities.

The share of direct and portfolio equity in external liabilities has been increasing. An important part of the increase in equity liabilities is due to capital gains by foreign holders. In many developing countries, presence in equity markets is greater than that in the United States and Japan.

While still remaining below the levels seen a decade ago as a percentage of gross domestic product (GDP), external debt buildup has accelerated since the crisis in 2008. This is mainly due to borrowing by the private sector, which now accounts for a higher proportion of external debt than the public sector in both international bank loans and security issues. A very large proportion of private external debt is in foreign currency. There is also a renewed tendency for dollarization in domestic loan markets.

As a result of a shift of governments from international to domestic bond markets and opening them to foreigners, the participation of non-residents in these markets has been growing.

The proportion of local-currency sovereign debt held abroad is greater in many developing countries than in reserve issuers such as the United States, the United Kingdom and Japan. It is held by fickle investors rather than by foreign central banks as international reserves.

International banks have been shifting from cross-border lending to local lending by establishing commercial presence in developing countries. Their market share in these countries has reached 50% compared with 20% in developed countries. These banks tend to act as conduits of expansionary and contractionary impulses from global financial cycles and increase the exposure of developing economies to financial shocks from advanced economies.

Strategic integration

One of the key lessons of the history of economic development is that successful policies are associated not with autarky or full integration into the global economy, but strategic integration seeking to use the opportunities that a broader economic space may offer while minimizing the potential risks it may entail. This is more so in finance than in trade, investment and technology.

For one thing, the international financial system is inherently unstable in large part because multilateral arrangements fail to impose adequate discipline over financial markets and policies in systemically important countries which exert a disproportionately large impact on global conditions.

For another, the multilateral system also lacks effective mechanisms for orderly resolution of financial crises with international dimensions. Thus, closer integration of several emerging and developing economies into the international financial system in the past 10 years, after a series of crises with severe economic and social consequences, is a cause for concern.

In all likelihood, these countries will be facing strong destabilizing pressures in the years ahead as monetary policy in the United States returns to normalcy after six years of flooding the world with dollars at exceptionally low interest rates.

In weathering a possible renewed instability, they cannot count on the more flexible currency regimes they came to adopt after the last bouts of crises or the reserves they have built from capital inflows or the reduced currency

exposure of the sovereign.

It is important that they, as well as the international community, avoid going back to business-as-usual in responding to a new round of financial shocks, bailing out investors and creditors and maintaining an open capital account at the expense of incomes and jobs.

They need to include many unconventional policy instruments in their arsenals to help lower the price that may have to be paid for the financial excesses of the past several years. They should also take the occasion to rebalance the pendulum and to bring about genuine changes in the international financial architecture. *(IPS Columnist Service)* ❐

Yilmaz Akyuz is chief economist at the South Centre in Geneva. The views expressed in this article are those of the author and do not necessarily represent the views of, and should not be attributed to, IPS - Inter Press Service. This article is based on "Internationalization of Finance and Changing Vulnerabilities in Emerging and Developing Economies", South Centre Research Paper No. 60, January 2015, available at www.southcentre.int/research-paper-60-january-2015.

Is debt relief for Ebola-stricken countries enough?

Debt relief granted by the IMF to the Ebola-hit countries Guinea, Liberia and Sierra Leone falls short of what is needed, say debt campaigners, especially given concerns over new loans and the conditions that will come attached.

by Bodo Ellmers

The International Monetary Fund (IMF) has announced its intention to cancel almost $100 million of debt owed by the Ebola-affected countries Guinea, Liberia and Sierra Leone, and will also provide $160 million in new loans. Debt justice campaigns welcomed the move, but have demanded that the IMF and other creditors should cancel all outstanding loans. Moreover it is still unclear whether the IMF has learnt any lessons regarding the quality of its programmes: health experts have expressed harsh criticism over the impact of IMF conditionality on affected countries' ability to prevent the Ebola outbreak in the first place.

Partial debt relief announced

Debt cancellation campaigners celebrated a small victory on 5 February as the IMF finally announced that $95 million in outstanding IMF loans to Guinea, Liberia and Sierra Leone will be cancelled. This debt relief is part of an assistance package of $300 million in "debt relief, grants and loans" that the G20 grouping of major economies pledged last November. It is financed through a new IMF facility called the Catastrophe Containment and Relief Trust.

While the IMF's gesture was appreciated by many, as it relieves the affected countries from debt repayments to the IMF over the next years, observers argued that the IMF could have reacted earlier and should have cancelled all debt. The current debt of Guinea, Liberia and Sierra Leone to the IMF amounts to $410 million. A full debt cancellation could have easily been financed through the IMF's $9 billion in reserves that it has accrued through high interest rates on its loans, primarily to crisis-hit European countries such as Greece in recent times.

Abu Bakarr Kamara from the Budget Accountability Network in Sierra Leone argued: "The debt relief by IMF is a welcome one for Sierra Leone. However, the devastation caused by Ebola on our health system requires sustained and progressive investment in the health sector for the next five years. Cancelling all Sierra Leone's debt would contribute greatly to improve our health systems hence contributing towards achieving the Millennium Development Goals."

Jubilee USA, which has campaigned heavily for debt cancellation, states that the three countries have a combined total debt stock of over $3 billion, so the recently announced relief is just a drop in the ocean. It has also stressed that "much of that debt comes from dictatorships, civil wars and one-party rule".

New loans are not the answer

The debt relief is complemented by a new assistance package which consists mainly of new loans, although many civil society organizations have argued that only grant assistance can help the West African countries to build and sustain effective health systems.

Tim Jones, a policy officer at Jubilee Debt Campaign, found that the new loans will quickly outweigh the positive impact of debt relief: "The lending of more money means that Guinea, Liberia and Sierra Leone's debt will actually increase. Grants should be given to cope with the impact of Ebola, not more loans which leave an unjust debt to be repaid over the next decade."

The IMF announced that it will provide $160 million in new loans as part of this package, and on top of earlier commitments. Because of the new loans, the debt of Guinea, Liberia and Sierra Leone to the IMF will increase from $410 million to $620 million over the next three years despite the debt relief.

This is worrying, as these figures suggest that the countries will remain subject to IMF conditionality – which has had devastating impacts in the past – for many years to come.

Conditionality revisited?

In November last year, a group of researchers from British universities published a much-debated article in *The Lancet*. They found that the weakness of the health systems in the West African region was a key reason for the rapid spread of the Ebola outbreak. All three affected countries were under IMF programmes at the time of the outbreak. In fact, since 1990, the IMF has provided support to Guinea, Liberia and Sierra Leone for 21, 7 and 19 years respectively.

The scholars argued that the IMF programmes, more precisely the conditionality attached to them, contributed to the weak health systems through three channels: the overall fiscal constraints imposed on the borrower countries; reductions in public sector employment; and the premature decentralization of health policy.

IMF staff who spoke to the European Network on Debt and Development (Eurodad) argued that the IMF sets primarily macroeconomic targets and it is up to the borrower countries to decide on spending priorities. However, the *Lancet* authors found that all countries met the macroeconomic targets – which entailed prioritization of debt service and bolstering of foreign exchange reserves – while they missed social spending targets because public resources turned out to be insufficient to fund all areas. They also pointed to counterproductive micro-interventions by IMF staff, for instance

discouraging Sierra Leone's "Free Health Care Initiative" of 2010 due to its fiscal implications.

While full debt cancellation is one priority for the IMF to deliver, the Ebola lesson should also trigger a review of IMF programme design and conditionality policy. ❐

Bodo Ellmers is Policy and Advocacy Manager with Eurodad (European Network on Debt and Development). This article is reproduced from eurodad.org.

(continued from page 9)

is a low currency level. But other countries can similarly defend their actions.

The proposed US law, if it takes effect, can thus trigger trade protection measures and retaliation.

Another casualty could be the TPPA, which already contains unpopular and controversial components such as an investor-state dispute system, tight intellectual property rules, the opening up of government procurement, and curbs on state-owned enterprises.

If the US Congress persuades the administration to include punishment for currency manipulation as another TPPA component, it might be just too much, like the straw that broke the camel's back. ❐

Martin Khor is Executive Director of the South Centre, an intergovernmental think-tank of developing countries, and former Director of the Third World Network. This article first appeared in The Star *(Malaysia) (16 February 2015).*

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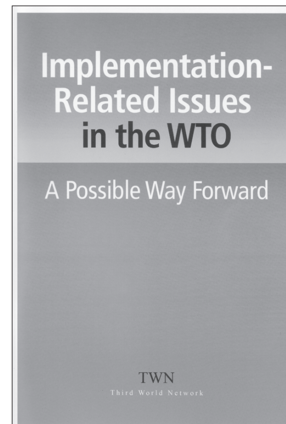
Implementation-Related Issues in the WTO: A Possible Way Forward

The set of multilateral agreements under the jurisdiction of the World Trade Organization (WTO) governs the conduct of international trade. Implementation of the commitments imposed by these agreements has, however, given rise to a host of problems for the WTO's developing-country members, ranging from non-realization of anticipated benefits to imbalances in the rules.

These implementation-related issues have been on the WTO agenda for over a decade, yet meaningful resolution is still proving elusive. This paper documents the progress – or, more appropriately, lack thereof – in the treatment of the implementation issues over the years. It looks at the various decisions adopted, to little effect thus far, by the WTO in this area, including the 2001 Doha Declaration which incorporates the implementation issues into the remit of the ongoing Doha round trade talks.



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The paper exhorts the developing countries to draw upon the Doha mandate to bring the implementation issues back to the centrestage of negotiations. As a practical measure given the resource constraints developing-country negotiators face in the WTO, it is proposed that the implementation issues be taken up according to a suggested order of priority. Prioritization notwithstanding, the paper stresses that developing countries have every right to seek solutions to each of these longstanding, long-neglected issues.

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Analysis

Developing-country interests sidestepped in FSB proposals

Andrew Cornford **runs the rule over proposals advanced by the Financial Stability Board concerning resolution procedures for and loss-absorption capacities of global systemically important banks.**

The proposals of the Financial Stability Board (FSB) on measures to end "Too-Big-To-Fail" (TBTF), through procedures for resolution of banks and strengthening balance sheets to protect taxpayers in respect of the global systemically important banks (G-SIBs), do not appear to cover or meet the need to counter systemic risks of developing countries and their institutions in cross-border insolvencies involving other SIBs.

One outcome could be that countries might decide to ensure subsidiarization as the corporate form for cross-border banks, since this choice may be more protective of a country's interests owing to the way in which the losses of an insolvent cross-border banking group are assumed in the jurisdictions in which loss-making entities are legally incorporated.

Background

At the Pittsburgh Summit of the G20 major economies grouping in 2009, there was agreement that the FSB should propose measures addressing the risks associated with the operations and insolvency of systemically important financial institutions (SIFIs).

Amongst such institutions, special attention was directed at systemically important banks (SIBs) owing to the damage which the failure of such banks can inflict on economies and to the implicit subsidy which is entailed by the likelihood that in the event of insolvency or the threat of insolvency governments will have no option but to provide public funds to control such damage and the financial instability which it can cause.

The underlying rationale of the regulation of banks is to enable them to support productive economic activities, to prevent instability and crises with their social and economic costs, and – in the event of a banking crisis – to mitigate the risks and severity of systemic failure. This role holds for SIBs as well as for banks which are not classified as systemically important.

But SIBs have features which give the pursuit of these objectives by policymakers and regulators special importance. These features are their size and their inter-relationships with other financial and non-financial entities. They have taken on special importance in a world of cross-border banking. The cross-border dimension has complicated the regulation of SIBs since the regulations of more than one national regime are involved.

In a report of September 2013 (FSB, "Progress and Next Steps Towards Ending 'Too-Big-To-Fail'", Report of the Financial Stability Board to the G20, 2 September 2013), the FSB reviewed progress made since regulators had to confront the daunting lack of coherent planning, preparation and frameworks for dealing with the widespread post-2008 distress and insolvency amongst major banks.

The complexity of the resulting problems can be grasped from data concerning Lehman Brothers Holdings at the time of its bankruptcy in September 2008. The group had over 2,000 affiliates in a single integrated enterprise in over 40 countries (H.S. Scott and A. Gelpern, *International Finance: Transactions, Policy and Regulation*, nineteenth edition, Thomson Reuters/ Foundation Press: 319). The failure led to a large number of judicial and administrative proceedings in many different jurisdictions. Moreover, it triggered default clauses in derivatives contracts which allowed Lehman's counterparties the option of terminating contracts and seizing collateral, actions which were legal but complicated the task of administering the insolvency. The United States bankruptcy procedures for Lehman lasted three years, the plan for paying the firms' creditors being confirmed only in December 2011.

Progress and outstanding issues

At the global multilateral level, the progress reviewed in the FSB's report of September 2013 included a number of steps: the designation of 28 G-SIBs to which higher capital requirements will apply; recommendations as to tighter procedures for risk management and risk reporting; and agreement on measures regarding the improvement of the infrastructure for financial markets such as central counterparties for derivatives to reduce the risk of contagion throughout the financial system due to defaults by individual counterparties. (Central counterparties mutualize credit risks associated with contracts between bilateral counterparties by assuming one side of, and guaranteeing performance of, all open contracts.)

The report also drew attention to ongoing initiatives at the national or regional (EU) levels directed at structural reforms for the banking sector. Important issues which had still to be fully addressed were service-level agreements which assure the continuity of crucial services where chains of transactions involve insolvent firms and the staying of early termination of financial contracts in insolvencies which, although legal, can hinder the implementation of resolution strategies for cross-border banks.

Owing to their complexity and political sensitivity, two subjects considered by the FSB to be of critical importance to the regulation and resolution in insolvency of G-SIBs are requiring a predictably long process for the development of rules capable of achieving consensus among the G20's membership: (1) resolution strategies and procedures for G-SIBs at the institution level, and (2) additional resources for the absorption of losses by a G-SIB sufficient to avoid a bailout with public funds.

The FSB's recent work on these two subjects is the principal focus of what follows. Although the focus of the FSB's work is on resolution and loss absorption, the proposals would also

be expected to reduce the likelihood of distress and insolvency.

Key features of resolution

The essential elements of the FSB's agenda regarding resolution were published in an FSB report of 2011 (FSB, "Key Attributes of Effective Resolution Regimes for Financial Institutions", October 2011). The document, henceforth referred as the Key Attributes, was updated in October 2014.

The recommendations of the Key Attributes cover not only banks' resolution strategies and procedures but also features of appropriate legal and institutional regimes within which the strategies and procedures can be successfully implemented. Thus, the Key Attributes cover the following: the powers of resolution authorities; the setting-off and collateralization of banks' positions, and the segregation (and thus the protection) of individuals' assets; safeguards of the interests of creditors; the funding of firms in resolution to avoid reliance on public ownership and public bailout funds; the legal framework for cross-border cooperation between resolution authorities in different jurisdictions; the establishment of crisis management groups for cross-border SIBs; institution-specific cross-border cooperation agreements; regular assessments by resolution authorities of the feasibility and credibility of G-SIBs' resolution strategies; ongoing processes of planning for resolution and possibly recovery; and ensuring that there are no legal, regulatory or policy impediments to the cross-border exchange of necessary information between resolution authorities in different jurisdictions.

Alternative approaches to resolution

The first of the subjects discussed in this article starts from the choice of single point of entry (SPE) versus multiple point of entry (MPE) for resolution of G-SIBs. Resolution strategy thus involves a bank's corporate form and its business model or strategy. The second subject (described in the following section) concerns the size and form of loss-absorbing capacity beyond the capital requirements additional to those of Basel III which G-SIBs must already meet.

Under SPE resolution (which generally presupposes a centralized model for a cross-border bank with a group consisting of branches), the authority of the parent institution manages the overall process of resolution. Under MPE resolution, the host supervisors of the jurisdictions where there are subsidiaries play key roles in resolution.

Although in the Key Attributes the FSB devotes greater attention to the mechanics of the SPE process, it avoids explicitly taking a position in favour of the SPE over the MPE process, thus acknowledging that the corporate form in which banking entities are given market access to different jurisdictions should allow for the policy choice of subsidiarization owing to the perceived need for national regulatory control.

Supporters of SPE resolution draw attention to what they consider to be the advantages of branches (the corporate form usually associated with this approach) from the point of view of both operational efficiency and the facilitation of resolution. The branch-based model is viewed as facilitating the flow of capital and liquidity in accordance with directives from an integrated organizational and risk management. Unsurprisingly, the managerial autonomy provided by this model means that it is favoured by major international banks and lobbies such as the Institute of International Finance.

Resolution, supporters of this model maintain, is facilitated by the SPE approach owing to the key role played by the authority of the parent entity. Thanks to the support of the parent entity all the constituent companies should remain solvent, their liquidity is assured by intra-group financial flows, and the critical functions of the group (i.e., systemically important financial services such as payments, settlement and clearing functions) continue to operate. Moreover, the SPE approach based on cross-border branching maximizes the likelihood of international cooperation.

As the Institute of International Finance, a lobby group for large banks, puts it in a recent report, "By requiring the local operation to subsidiarize, the host authority does extend its powers over it. However, the cost of this subsidiarization is that local creditors are potentially deprived of assets other than those of the local subsidiary" (Institute of International Finance, "Achieving Bank Resolution in Practice: Are We Nearly There Yet?", Washington, DC, September 2014: 15).

The trouble with this portrayal of the SPE approach's potential is that it is idealized. Such smooth cooperation between the entities – branches and parent institutions – of major groups does not correspond to much recent experience, where many of the steps actually taken were belated responses to crisis and required extensive intervention by national regulators.

Recent moves towards greater reliance on subsidiarization in several jurisdictions indicate that major national regulators are not convinced of being able to count on a favourable outcome for the SPE approach. According to this view, the high level of mutual trust required for the success of reliance on branch-based models during banking crises often does not exist. Moreover, clear legal obligations on parent institutions to holders of the liabilities of its branches are lacking.

The International Monetary Fund (IMF), while acknowledging the cost advantages of cross-border branching for some categories of banking group (in particular for those with primarily wholesale operations), has nonetheless drawn attention to the advantages of the subsidiary structure for the purpose of crisis management and resolution during banking crises (J. Fiechter, I. Otker-Robe, A. Ilyina, M. Hau, A. Santos and J. Surti, "Subsidiaries or Branches: Does One Size Fit All?", IMF Staff Discussion Note, 7 March 2011: Chapter II).

In the IMF's view, the ideal solution for tensions in cross-border banking relations consists of joint arrangements by the supervisors of parent and host countries, harmonized cross-border resolution regimes, and effective arrangements for burden sharing in stressed and crisis conditions. These are features which its supporters claim for the SPE approach. However, as the IMF notes, practical difficulties of cross-border cooperation during crises have led to the exploration by policymakers in several countries of the benefits of regulatory self-sufficiency of cross-border banks' local operations, regardless of whether the institution's business model is wholesale or retail banking.

Host countries' authorities can ensure that local subsidiaries have sufficient capital and liquidity in the country, thus minimizing the possibility of risks to financial stability being imported from related banking entities abroad in distress and

increasing the resources at the authorities' disposal in cross-border insolvencies – if necessary through recourse to ring-fencing local banking entities.

The reduced freedom of management as to the location of capital and liquidity associated with subsidiarization can thus actually be an advantage and not a disadvantage as supporters of the branching model argue. Moreover, subsidiarization facilitates the selling-off by resolution authorities of a cross-border bank's local constituent entities and the implementation of "living wills", i.e., the recovery and resolution plans for the winding-down of systemically important financial groups if they fail.

Increasing loss-absorption capacity

Increasing the loss-absorption capacity of G-SIBs is the subject of a FSB consultative document of November 2014 containing detailed proposals (FSB, "Adequacy of loss-absorbing capacity of global systemically important banks in resolution", Consultative Document, 10 November 2014). Noting that the FSB's proposals would bail in – i.e., impose losses on – certain categories of a bank's liabilities as part of increasing loss-absorbing capacity, some commentators apprehensively – but mistakenly in the context of the FSB's plans – recalled losses imposed on depositors as part of measures taken in response to the economic and financial crisis in Cyprus in 2013.

This crisis followed Cyprus's membership of the EU from 2004 and of the monetary union from 2008. These were accompanied by a doubling of the size of the financial sector between 2006 and 2011. The financial bubble, which included pouring of money into high-risk ventures abroad and extensive exposure to the Greek banking system, was eventually followed by collapse. The response of the Cypriot government, supported by EU finance ministers, initially included a tax on bank deposits including those of smaller savers. Amidst a storm of protest, which was not limited to Cyprus, the tax was rescinded in favour of the writing-down of large deposits through measures such as their conversion into equity. These policy interventions came with the price of a public-relations blow to belief in the safety of deposits in EU banks (D. Marsh, *Europe's Deadlock: How the Crisis Could Be Solved – and Why It Won't Happen*, New Haven and London, Yale University Press, 2013: 53-57).

The FSB's proposals on loss absorption (which, as noted, are still at the consultative stage and are directed at TBTF banks) would not lead to the writing-down of retail deposits. Indeed, as explained below, one of the aims of the proposals is to maintain the banking system's capacity for carrying out critical functions (defined earlier), which would not be compatible with a major disruption of retail banking.

This implies only that depositors are protected from losses in their role as depositors. To the extent that the resolution procedures and the loss-absorbing capacity for G-SIBs introduced in response to the FSB's proposals do not cover losses in insolvencies, the losses would still be met by much the same group in their role as taxpayers. But the distribution of these losses would be for governments to decide.

In its report of September 2013, the FSB committed itself, in consultation with standard-setting bodies, to the preparation of proposals on the adequacy of the loss-absorbing capacity of G-SIBs in resolution (what it calls "gone concern loss absorbing capacity" as distinct from the "going-concern capacity" required to keep it out of insolvency).

The implication of this commitment was that the FSB was sceptical that the supplementary capital requirements prescribed for G-SIBs in Basel III would be sufficient to guarantee a resolution strategy which "mitigates risks to financial stability, ensures continuity of critical functions and minimizes taxpayers' exposures to losses", as the General Manger of the Bank for International Settlements has put it (J. Caruana, "How much capital is enough?", address to the IESE Business School conference on "Challenges for the future of banking, regulation, supervision and the structure of banking", London, 26 November 2014).

The FSB document of November 2014 covers proposals concerning the amount of total loss absorption capacity (TLAC) required, arrangements which will ensure its availability in the resolution of cross-border banking groups, the eligibility of financial instruments for inclusion in TLAC, the interaction of TLAC with pre-existing capital requirements, transparency, and restrictions on holdings of TLAC to avoid contagion risks if the holdings are exposed to loss during resolution.

The proposed minimum Pillar 1 TLAC requirement is in the form of a range of 16-20% of risk-weighted assets (RWA). The references to Pillar 1 and RWA are from Basel III itself and refer to a bank's exposures to credit risk (through its RWA) under different headings (loans, mortgages, off-balance-sheet commitments, etc.), as estimated in accordance with Basel III's rules, and to the minimum capital requirements corresponding to a bank's total exposure. Pillar 2 TLAC requirements consist of TLAC above the Pillar 1 minimum which is set in accordance with discretionary rules of national regulators.

Under the FSB's proposal, TLAC will include the principal capital instruments which count towards the fulfilment of Basel III minima but not the supplementary capital buffers (conservation, countercyclical, and designed to produce additional loss-absorbency for a set of G-SIBs designated by the FSB). The proposal also includes rules to ensure that all the entities in the banking group (parent holding company or companies and subsidiaries) will have adequate TLAC.

Instruments eligible for inclusion in TLAC must meet various legal conditions such as the following: the authorities must possess the legal powers to expose the TLAC-eligible liabilities to loss without the risk of a successful legal challenge or the possibility of compensation costs; and the authorities must be confident that holders of TLAC instruments are able to absorb losses during periods of stress in financial markets without spreading contagion or without the necessity of the allocation of losses to liabilities where the results could be the disruption of critical financial functions or significant financial instability.

Avoidance of contagion and of the disruption of critical financial functions implies, for example, that eligible TLAC must not include insured deposits, liabilities callable on demand without supervisory approval, and tax liabilities. Limitation of contagion is to be achieved through appropriate prudential restrictions such as dis-incentivizing the holding of TLAC issued by other G-SIBs. Meeting these conditions will require clarity about priorities in the order in which TLAC instruments will absorb losses in a resolution, and thus dis-

closure to holders and potential holders.

Concluding comments

This article has been principally concerned with only two of the many issues covered in the FSB's coverage of measures to end TBTF. Procedures for the resolution of banks and the strengthening of their balance sheets to protect taxpayers in bank insolvencies are not of course limited to the banks classified as G-SIBs by the FSB, even though the systemic risks of failure on the part of these banks are particularly great.

As a result of the restrictions in the coverage of the FSB's list, with the exception of a small number of Chinese banks (Agricultural Bank of China, Bank of China, Industrial and Commercial Bank of China Limited), institutions with parents in emerging market and developing economies (EMDEs) are not included, though of course the failure of an FSB G-SIB would be likely to have ripple effects in EMDEs.

Limitations on the direct relevance of the FSB's proposals to EMDEs are acknowledged in the FSB's proposals. Indeed, G-SIBs headquartered in such markets will not initially be subject to the Common Pillar Minimum TLAC requirement (FSB, "Adequacy of loss-absorbing capacity of global systemically important banks in resolution": 14). This makes sense since the Chinese banks listed in November 2014 by the FSB among G-SIBs (Agricultural Bank of China, Bank of China, Industrial and Commercial Bank of China Limited) are state-owned so that their liabilities are not held by parties whose bailing-in will contribute to avoiding losses to taxpayers (who would anyway have to meet the costs of such a bank's distress or failure).

Many of the guidelines proposed for G-SIBs would in fact be relevant in cross-border insolvencies of smaller banks from both EMDEs and advanced economies. In its report of September 2013 (FSB, "Progress and Next Steps Towards Ending 'Too-Big-To-Fail'": 16), the FSB also refers to the framework for the TBTF problem for D(domestic)-SIBs developed by the Basel Committee on Banking Supervision (BCBS, "A framework for dealing with domestic systemically important banks", October 2012), whose rules are pertinent for banking sectors in EMDEs.

This framework would be "based on the assessment conducted by the local authorities, who are best placed to evaluate the impact of failure on the local financial system and the local economy". An implication of this point is that "in order to accommodate the structural characteristics of individual jurisdictions, the assessment and application of policy tools should allow for an appropriate degree of national discretion". While the framework for D-SIBs does cover higher loss absorbency, it does not include resolution procedures.

A consequence of the FSB's focus on TBTF institutions in the documents discussed in this article is that its treatment of systemic risk is limited to that which results from the many forms of economic inter-relatedness of such institutions with other banks and with non-financial firms. But systemic risk is not limited to risks due to such inter-relatedness. A dissent to the report on the financial crisis of the United States Financial Inquiry Commission (National Commission on the Causes of the Financial and Economic Crisis in the United States, Final Report: 433) notes that systemic risk is also associated with situations characterized by the effects of correlated failures: "In a common shock, the failure of one firm may inform us about the breadth or depth of the problem, but failure of one firm does not cause the failure of another." Correlated failures, such as those due to external payments-cum-banking crises, may frequently be more important sources of systemic risk in EMDEs than the inter-relatedness of large financial institutions.

Both sorts of systemic risk – those due to the inter-relatedness associated with TBTF institutions and those due to correlated failures – could present a threat to banks' maintenance of critical functions, including functions on which retail banking depends. Hence, insured deposits and liabilities called on demand without supervisory approval are excluded from the bailing-in features of TLAC in the FSB's proposals.

One feature of the FSB's proposals is the way in which they evade a problem which has stymied previous initiatives to achieve agreement on procedures for the resolution of large cross-border banks. This problem concerns procedures for distributing losses between the different jurisdictions involved. The belief which was the source of these difficulties was that much of the losses would have to be met by public sector or cooperative institutions rather than the failed banks, and that agreement was thus necessary on how these losses would be distributed internationally.

The assumption of the FSB's proposals would appear to be that the losses could be completely borne by resources available through the bailing-in of selected classes of holders of loss-absorbing liabilities. This may be over-optimistic, and even after the bailing-in there may remain significant losses which must still be distributed between different groups and jurisdictions.

The lack of such optimism among regulators helps to explain countries' increasingly favourable view of subsidiarization as the appropriate corporate form for cross-border banks, since this choice can be protective of a country's interests owing to the way in which the losses of an insolvent cross-border banking group are assumed in the jurisdictions in which loss-making entities are legally incorporated. *(SUNS7967)* ❒

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