

Confidential

Mr. Harold

A PROPOSAL FOR AN INTERNATIONAL COMMERCIAL UNION

I. OUR POST WAR COMMERCIAL PROBLEM

1. The United Kingdom will be in a difficult commercial position after the war. As a community we depend upon imports of essential foodstuffs and raw materials, which we must purchase by the export of manufactured goods. Development during the war, such as the loss of income from foreign investments, will have increased our need for an expanded export trade, while at the same time the industrialisation which has taken, or is likely to take place in certain overseas territories may well have restricted some of our export opportunities. We import essentials; we export goods with which our customers can more easily dispense. If ever there was a community which had an interest in the general removal of restrictions to international commerce, it is the United Kingdom. It is true that the United Kingdom as a large purchaser of many commodities, is in a strong bargaining position. But use of this bargaining power in a discriminatory manner would be economically less advantageous to us than a general expansion of our overseas markets, and, politically, would endanger the possibility of Anglo-American co-operation.

2. Our trade in the past has been very largely of a multilateral character. We have bought goods from the United States with income obtained from the sale of our produce in other less well developed territories. If many of our most readily available sources of supply of essential imports are not to be closed to us, it is important that the opportunities for beneficial multilateral trade should be preserved to their fullest extent.

3. Our export possibilities would thus be directly and indirectly greatly improved, if we could obtain the agreement, for example, of the United States to modify its pre-war excessive tariff barriers and of Germany to give up its pre-war policy of bilateralism and trade discrimination. These considerations suggest that we, above all other countries, stand to gain (i) from a policy of general world economic and financial expansion which will maintain a high level of buying power in export markets, (ii) from a general reduction of barriers and restrictions in international markets and (iii) from a removal of those discriminations and rigidly bilateral bargains which remove the opportunities for multilateral trading.

4. Multilateral trading and the removal of trade restrictions do not, however, imply laissez-faire, and are in no way incompatible with a system of state trading. We shall wish to co-operate with the United States, on the basis of Article VII of the Mutual Aid Agreement of 23rd February, 1942, on "action by the United States of America and the United Kingdom, open to participation by all other countries of like mind, directed to... the elimination of all forms of discriminatory treatment in international commerce, and to the reduction of tariffs and other trade barriers..." At the same time we must aim at the formulation of such action by means, which do not automatically preclude countries such as the U.S.S.R. which may be assumed to desire to continue a system of state trading nor prevent us, if we so desire, from continuing a system of state importation for certain products.

5. After the war we shall not be in a position in which we can afford unconditionally to abandon all protective devices. We cannot readily indulge in a unilateral policy of removing our protective armour and shall thus desire to retain the right to restrict purchases from, and to discriminate against, those countries which themselves retain highly protective commercial policies or which discriminate against us. We shall, moreover, need to retain the right to impose more general restrictions on purchases of inessential goods or on unnecessary payments abroad so long as we are faced with an acute problem of restoring equilibrium to our international balance of payments.

6. The essential features of our post-war commercial problem may, therefore, be summarised as follows:-

(i) We shall need a large expansion of our export trade and shall stand to gain very greatly from a, world system in which there is a general expansion of world purchasing power and in which restrictions and discriminations on foreign trade are reduced or removed.

(ii) Apart from our interests we are committed under Article VII of the Mutual Aid Agreement to such a policy, and the future of our relations with the United States requires that we should implement this undertaking.

(iii) We need, however, to implement these undertakings in a way which leaves room for state trading and which does not preclude us (a) from imposing restrictions or discriminations against those countries which impose severe restrictions or discriminations against us or (b) from restricting our payments to other countries if and when balance of payments difficulties make such action inevitable.

7. We must, however, consider these problems in the special setting of Anglo-American conversations. From the point of view of the United Kingdom it is essential that priority should be given to proposals of a monetary character for the adjustment of international balances of payments and to suggestions for ensuring a general expansion of world markets. But it is equally important that the United Kingdom, if for no other reason than to remove any doubts that may exist in American minds, should be in a position to make positive proposals in the commercial field for a general reduction of trade restrictions and discriminatory practices. It is, moreover, important that proposals in this sphere should continue the reduction of trade restrictions with the reduction of discriminatory practices; for the United Kingdom has more to gain from the power and the United States more from the latter. The following paragraphs of this memorandum have been written with these considerations in mind.

II. THE CONTRIBUTION OF OTHER PROPOSED INSTITUTIONS TO THE SOLUTIONS OF THE COMMERCIAL PROBLEM

8. The proposals which have already been made (R.P.(42)2 paragraphs 61-134) for the institution of an International Clearing Union, if they are adopted, should much simplify our tasks in formulating far-reaching and imaginative proposals for the reduction of restrictions to international commerce.

9. In the first place, these and similar proposals would greatly help - indeed this is the essence of the proposals - to adjust the balance of payments without undue strain on the debtor countries. Since a large number of protective devices are in origin essentially weapons of defence of countries which are faced with an undue pressure on their balances of international payments, an effective mechanism which makes the creditor nations responsible for a due part of adjustments of international payments should clear the way for attempts to mitigate protectionism.

10. But, in the second place, the machinery of the Clearing Union, through the debit and credit balances of its members, provides an effective and automatic measurement of existing maladjustments in balances of payments. A country which claims that it must be permitted to impose certain protective restrictions as a result of a serious maladjustment in its balance of payments can appeal to (or be referred to), a reasonably unambiguous index, - its debit balance with the Clearing Union. It should, for example, be possible for a country to commit itself in commercial agreements to remove various protective devices but, at the same time, to reserve the right to reimpose some of these devices when and for as long as its debit with the Clearing Union was in excess of a certain figure.

11. Thirdly, the Clearing Union, may be expected to aid in promoting that general expansion of demand in world markets which, in Article VII of the Mutual Aid Agreement itself, comes before the removal of trade restrictions and discriminations as an objective of international co-operative action. Indeed, it is only in a general milieu of economic expansion that the pressure on the balance of payments of debtor countries is likely to be sufficiently relieved to make possible a really effective lowering of protective devices. There are other proposals under consideration which will help towards the same purpose of economic expansion. In particular, the proposals for the development of international investment (R.P.(42)2 paragraphs 178-195) and the proposals for a systematisation of buffer stock arrangements for primary products (U.S.E.(42)15) should provide effective support to an expansive international policy.

III. OUTLINE OF A POSSIBLE COMMERCIAL UNION

12. It is suggested, therefore, that the United Kingdom should propose the formation of an International Commercial Union for the purpose of achieving a general reduction of restrictions on international commerce. The Commercial Union would be founded on the following principles:-

- (i) Membership of the Union would be open to all states which applied for membership and which were willing to carry out the obligations of membership.¹ Membership of the Commercial Union would not be confined to members of the Clearing Union (just as membership of the Clearing Union would in no way be confined to members of the Commercial Union); but, as is indicated in (iv) below, members of the Commercial Union who were also members of the Clearing Union would obtain certain privileges in the Commercial Union.
- (ii) Members of the Commercial Union would undertake not to grant preferences or other price advantages to any other member of the Union without extending it to all members, except that certain moderate and defined degrees of preference might be given as between members of a recognised political or geographical group of nations. A clause of this kind would permit discrimination of any degree desired against countries which were not members of the Commercial Union and which had not, therefore, pledged themselves in turn not to discriminate. It would also permit discrimination of a defined and moderate degree in favour of a recognised political or geographical grouping of states, and would thus permit the continuation of a moderate degree of Imperial Preference.
- (iii) Members of the Commercial Union would undertake to remove altogether certain protective devices against the commerce of other members of the Union and to reduce to a defined maximum the degree of protection which they would afford to their own home producers against the produce of other members of the Union. A clause of this type would pledge members to eliminate or to limit their protective devices against other members of the Union who had undertaken a similar pledge, but would leave them free to introduce what protective measures they desired against non-members. Such an arrangement would be safeguarded by the right of any non-member state to join the Commercial Union.

¹ At a later stage when post-war international political arrangements are under discussion, it will, however, be a matter for consideration whether membership of the Commercial Union should not be confined to those states which are members of whatever international political organisation may be set up. For this would both provide a strong inducement to undertake the obligations of membership of the political organisation, and also would avoid the disruptive possibility that a member of the Commercial Union might discriminate in favour of fellow members of the Commercial Union against fellow members of the political organisation.

- (iv) Members of the Commercial Union, who were also members of the Clearing Union and whose accounts with the Clearing Union were in deficit by a certain defined amount, would be permitted to undertake certain special measures to meet the situation (cf. paragraph 14(vi) below).
- (v) The Charter of the Commercial Union would expressly state that state trading by members of the Union was not precluded. An indication should be given of the way in which the provisions of the Charter of the Commercial Union should be applied both in the case of competitive trading and in the case of state trading.
- (vi) The Charter of the Commercial Union would provide for the institution of an International Commerce Commission of a semi-arbitral semi-judicial nature. Members could refer complaints to this body in order to obtain an opinion whether the Charter of the Union was being broken by any particular action of a particular member of the Union.
- (vii) Membership of the Commercial Union would in no way preclude any member from concluding any type of commercial treaty or agreement with any other state - whether a member of the Union or not - provided only that the terms of the treaty or agreement were not incompatible with its obligations as a member of the Union.

13. If an attempt were made to draft a Charter for a Commercial Union of this type, one of the most important questions would be how precisely worded should be the definition of the discriminations and degrees of protection that would be disallowed to members of the Union and of the actions which would be permitted or disallowed to state trading organisations. It is in this connection that the major dilemma is to be faced. If an attempt is made to define very rigidly and precisely exactly what any member may or may not do in all possible circumstances, it is probably that as circumstances change and as states introduce new methods of trading organisation certain state measures may be precluded which it is not in the general intention of the Charter to disallow and certain other measures may be allowed which it is in the intention of the Charter to forbid. On the other hand, if the Charter is drawn up in much less precise terms and expresses only in the most general terms the types of protective device which it is intended to forbid and the general maximum degree of protection which it is intended to allow, then very great responsibility will rest upon the International Commerce Commission or similar body whose duty it was to interpret the Charter. The success of the Union will depend upon the formulation of the Charter in terms, which, on the one hand do not attempt to put international trade into an impossible strait jacket and, on the other hand, do not impose upon the International Commerce Commission such a burden of semi-legislative duties that it would not bear.

14. The following clauses are intended merely as an illustration of one possible set of conditions which might be included in that section of the Charter of the Commercial Union, in which the limitations on members' discriminatory or protective policy are defined:-

- (i) Members would be forbidden to discriminate (whether by means of taxes, subsidies, preferential prices offered by state organisations, or other means) in the prices offered for the produce of other members of the Union.
- (ii) Members would be bound to give other members of the Union as favourable prices for their produce as they gave for the similar produce from any non-member state.
- (iii) As exceptions to Clauses (i) and (ii) above members could give price preferences up to a maximum of, say, 10% to the produce of another state with which it formed a special recognised geographical or political union.
- (iv) Members would be forbidden to give a preference (whether by tax, subsidy, price offered by state trading body or other means) in price to their home producers which was more than, say, 25 per cent. greater than the price offered to similar goods produced by other members of the Union.
- (v) Members would be forbidden to impose quantitative restrictions or prohibitions, other than for reasons of public health or public safety, on the import of goods from other members of the Commercial Union.
- (vi) Members would undertake not to impose restrictions on payments for current (as exposed to capital) transactions to other members of the Union, except that a country which was also a member of the Clearing Union and was in deficit with the Clearing Union to a defined extent would be permitted to impose restrictions on current payments of a non-discriminatory and temporary character for as long as it remained in this position. The degree of deficit in the Clearing Union which gave this right to impose restrictions on current payments would be so defined that the Country in question would be simultaneously liable, on the recommendation of the Governing Board of the Clearing Union to take appropriate action to restore its balance of payments.

1. Such action is exemplified in paragraphs 85(4)(b) of R.P.(42)2 which suggests:- "As a condition of allowing a member - State to increase its debit balance in excess of a half of its quota, the Governing Board of the Clearing Union may require (i) a stated reduction in the value of the members currency, if it deems that to be the suitable remedy, (ii) the control of outward capital transactions if not already in force, and (iii) the surrender of a suitable proportion of any separate gold reserve it may hold in reduction of its debit balance".

(vii) Members would undertake not to impose quantitative restrictions or prohibitions on exports except as part of a recognised international regulation scheme for primary products (as arranged for in the scheme outlined in U.S.E.(42) 15).

(viii) Members would undertake not to impose open or hidden taxes of more than, say, 25 per cent. or subsidies of more than, say, 10 per cent. on exports to any country whether a member of the Commercial Union or not.

(ix) Members would undertake not to enter into any commercial treaty or agreement with any state which required that state to discriminate against any other member of the Commercial Union.

15. The purpose of these various provisions is clear. Clauses (i) to (iii) in the preceding paragraph would limit price discriminations for imports; Clause (iv) would limit the degree of price protection which could be given to home production; Clauses (v) and (vi) would prevent quantitative or value restrictions on imports, except in the case of countries in a "deficiency" position with the Clearing Union; and Clauses (vii) and (viii) would cover export policy, preventing both undue restriction of export and export dumping, - the latter of which may be equally obnoxious whether it be to other member states or to non-member states.

IV. THE PROBLEM OF STATE TRADING

16. The general principles of the application of these clauses to countries adopting a competitive trade organisation are clear, although there would, no doubt, be many difficult technical problems to be determined in border-line cases by the International Commerce Commission as to what exactly did or did not constitute a price preference or a restriction on payments. The problem of applying these clauses to cases of state trading would probably in practice present more difficulties since it is as yet a less familiar problem; but in principle it should be no less capable of satisfactory solution.

17. It resolves itself into a two-fold problem:-

(i) that of determining the degree of price preference or protection which is being offered by the state trading organisation and

(ii) that of deciding whether a quantitative restriction on imports (or on exports) is being imposed.

In the case of a state which, while its trading system is mainly competitive, monopolizes for itself the trade of a limited number of commodities, the problem of judging the degree of price discrimination or of price preference given as between one source of supply and another or as between one market and another does not present any additional difficulties of principle. This problem may become somewhat more complicated in practice, but it still remains in essence the same, even in the case of a country which has socialised trade in all or the majority of products; such extreme cases

are, however, in the post-war world likely to be relatively few in number; and they will be still less important from the point of view of their share in the total of international trade.

18. The regulation of price preferences is not, however, sufficient to prevent discrimination or protection. A state trading organisation might, for example, discriminate in favour of one source of supply as opposed to another by buying much in the first and little in the second, even though it paid a non-discriminatory price. It is necessary to determine what corresponds in the case of state trading to the obligations (suggested in clauses (v) - (vii) of paragraph 14 above) not to impose quantitative restrictions on imports or exports except in certain clearly defined cases. This limitation corresponds in the case of state trading to an obligation (i) to take from each foreign market as much imports as each such market would wish to supply at the price which the importing state organisation is offering and (ii) to sell in all foreign markets as much foreign exports as each such market would wish to purchase at the price at which the goods are offered by the state exporting organisation.

19. These considerations suggest that the principles of membership of the Commercial Union should be applied in such a way as (i) to impose the same obligations both to competitive and to state trading in all matters of price discrimination and price preference, (ii) to forbid in the case of competitive trading quantitative restrictions on imports and exports and on current payments, and (iii) to impose in the case of state trading obligations to purchase from, or to sell to, each foreign market as much as that foreign market wishes to sell, or to purchase, at the prices offered by the state trading organisation. It would, however, be a matter for detailed consideration to determine the extent to which, and the conditions on which long forward contracts could be entered into by state trading organisations within the framework of these principles. Such contracts should not be excluded; but they should be undertaken in such a way as to maintain a reasonable approximation to the principles outlined above.

V, THE INTERNATIONAL COMMERCE COMMISSION

20. The existence of some international body which had the competence to interpret the Charter of the Commercial Union, and to arbitrate or to give decisions in case of disputes among its members would be an essential part of the mechanism of such a union. It would, however, be premature at this stage to make detailed suggestions about the constitution of such a body. Its members should, no doubt, be appointed by the governments of the states making up the Commercial Union. It should, no doubt, have the power of expressing an opinion upon any complaint brought to its notice by one member of the Union against another member, and of requiring members of the Union to provide it with the statistical and other information necessary to form a judgment in such cases. It might well be ruled that, in such cases, its findings - both its majority and minority findings - should be published. But it is a matter for further consideration how far such findings should be binding on members of the Union. It might, for example, be provided, as a sanction against breaches of the Charter of the Union which refused to accept a majority finding of the Commission could be treated by other members as if it were no longer a member of the Union, in so far as the clauses prohibiting discriminatory practices were concerned. This, however, is a question which is probably best answered at a much later stage.

VI. THE PROBLEM OF THE TRANSITION

21. Membership of the Commercial Union, (at any rate on anything like the terms suggested above for illustrative purposes), would require an extensive re-adjustment of commercial policy in the case of a number of countries. If such major re-adjustments are desirable, there is much to be said for undertaking them after the cataclysm of a major war; for serious re-adjustments will be inevitable in such a period in any case, and it is surely better to re-adjust then to the conditions which are most desired than to rebuild to an ancient plan which it is intended in any case to reconstruct sooner or later. Economically there is much to be said for getting over the necessary adjustments quickly; and politically it may be wise to strike while the iron is hot and quickly to surmount the transitional difficulties at a time when the will for international collaboration is still great.

22. On the other hand, it may be impossible to suggest that this or any other country should commit itself to an immediate acceptance of all the principles of the Commercial Union immediately after the war. What would be required in this case is some transitional arrangement whereby countries can become members of the Commercial Union during a period after the close of hostilities on condition -

- (i) That they undertake to fulfil some of its obligations, such as the removal of quantitative import restrictions and prohibitions, within a short period of a year or two, and
- (ii) That they undertake to fulfil the remaining obligations within a period of not less than, say, five years. Such an arrangement might serve to secure that certain protective devices were quickly eliminated, that a more gradual movement was initiated for the removal or reduction of others, and - most important of all - that each member could plan its economic development on the assumption that within a specified number of years other members would have contracted their protective and discriminatory devices within reasonably precise and clearly defined limits.

(Int'd) J.E.M.

1ST AUGUST, 1942.