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WHEN LEVIATHAN COMES TO MARKET

Emerging multilateral disciplines on state owned enterprises and what existing rules on state trading enterprises and sovereign wealth funds can and cannot teach us.

Abstract

With the rise of China as a global economic power, only subscribing in part to the model of market capitalism, and with the rise - before China - of the so-called Asian tigers, all of which pursued state-led economic growth strategies, one needs to question whether the free-market consensus was even much of a consensus to start with. In fact, one does not have to go as far as Asia to see the statist model practiced in various degrees of intensity: Much of Europe, including of course Russia, never really lost its appetite for a big public sector, with varying degrees of direct and indirect interventions across a range of economic sectors (aerospace and energy to name just two). More than anything else, it was arguably the Global Financial Crisis of 2008 which did the most to put the nail in the coffin of any notion that the state must keep a healthy distance from the market, as governments all over the world leaped to the aid of various sectors of their economies in order to preserve jobs, maintain industrial bases, and in many cases, just keep the lights on.

One set of rules, adopted more than 60 years ago, to try and impose disciplines on governments when they intervene in markets as commercial actors, were those on state trading enterprises negotiated in the context of the Havana Charter for an International Trade Organization and which eventually came into force under the General Agreement on Tariffs and Trade (GATT). Another set of disciplines which have emerged more recently, are the Generally Accepted Principles and Practices of the International Working Group on Sovereign Wealth Funds, under the auspices of the International Monetary Fund, otherwise known as the Santiago Principles. The latest efforts to subject governments to some kind of discipline when they intervene as market actors are those currently being formulated at the OECD under the mantra of "competitive neutrality".

Underlying all these frameworks are some key concepts of how governments should comport themselves when they take their place alongside private-sector actors to contest markets as economic operators rather than overseers or regulators. This paper attempts to distill what these principles are, and to measure them against what can realistically be achieved in terms of policing the actions of sovereign countries under the inherently "soft" rules that characterize public international law.

Contents

I. FROM BEIJING TO WASHINGTON: CONFLICTING CONSENSUSES

A. Ideological Disclaimer and Statement of Intent

From the outset it should be stated that the author does not harbor any strongly held views on what the "right" degree of government intervention in a given market is. The purpose of this paper is not to advocate in favor of one of the various models that seem to be in contention, namely government-dominated versus market-driven economic governance. In fact, events over the recent years would seem to indicate that this is, if anything, a false choice. Market forces have an important role to play, just as do governments and institutions.

The topic that this paper seeks to address is what rules and disciplines - if any - governments have hitherto been prepared to allow themselves to be constrained by once they intervene on markets, not as regulators or overseers, but rather as just another (albeit important) set of market participants. We examine this issue on the basis of the existing rules on state trading enterprises under the GATT/WTO frameworks, as well as on the basis of those which have been adopted more recently pertaining to sovereign wealth funds under the auspices of the IMF. We also examine the disciplines emerging on state owned enterprises at the OECD and in the context of trade rules in various trade arrangements at the multilateral, regional and bilateral levels. In conducting this analysis, we will attempt to identify any commonalities in terms of principles that may engender over-arching themes, before discussing whether there is any genuine possibility of constraining sovereign actors under a legal system as inherently "soft" as public international law.

B. State Control versus the Market

Without wishing to engage in absurd generalizations or self-serving over-simplifications, the analysis pursued here is premised on two seemingly opposing poles or approaches to the role of government on markets.[1] The first of these recognizes the supremacy of market forces, and advocates, *inter alia:* freedom of competition between foreign and domestic firms (trade liberalization); privatization of state enterprises; deregulation and; the protection of property rights.[2] This approach, known more anecdotally as the "Washington Consensus", or less commonly as the "One-World Consensus"[3] later fell somewhat into disrepute as it came to be referred to as "neoliberalism" in Latin America or as "market fundamentalism" by other less sympathetic observers.[4]

The second of these approaches underlies an economic system where the guiding hand of the state is never far removed from any commercial activity. This second approach tends to be known as "authoritarian capitalism" and has more recently become known as the "Beijing Consensus".[5] Below, I spend some time discussing each approach briefly, before setting out what kind of government-led intervention into markets the analysis presented here seeks to address.

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1 For a more nuanced analysis of the highly differentiated continuum of various levels of state interventions in markets see, among others Schmidt (2009).

2 See Williamson (1990, updated in 1997) as summarized by Waelbroeck (1998); this approach is discussed in slightly more detail immediately below.

3 See Waelbroeck (1998) at p. 323.

4 See Williamson (2000) at p. 252.

5 It is worth noting here, that like Williamson's reference to the Washington Consensus, which he insists originally only referred to "the lowest common denominator of policy advice being addressed by the Washington-based institutions to Latin American Countries as of 1989" (Williamson [2000] at p. 251), the term "Beijing Consensus" also meant something different at the outset than how it has come to be understood in most policy circles today. Thus it is that the individual who is widely credited with coining the term, namely Joshua C. Ramo understood it to mean a set of three "theorems", the first being "a commitment to innovation and constant experimentation", the second being "rejection of per capita GDP as the be-all and end-all" and the last being "self-determination"; see Leonard (2006).

1. A Brief Introduction to the Free-Market Approach to Economic Governance

There seems to be, over time, the dawning of a realization, particularly in some important developing countries, that a number of policy approaches essentially favoring a market-based model of economic governance were increasingly the key to successful development instead of the state-led, import-substitution policies that many developing nations had adopted in their drive to achieve rapid industrialization following the Second World War[6]. For example, James Boughton, the well-known historian of the IMF, notes that as early as the mid-1980s Tanzania and Mexico both started moving away from what he terms "state socialism" or "government control over the economy" to more liberal economic policies, with Mexico joining the GATT in 1986. Boughton also points out that in India, Rajiv Gandhi had taken a similar approach, so that "[by] the end of the decade [the 1980s], economic liberalization had become a seemingly universal and unstoppable force."[7]

It was Williamson who in 1990 and again in 1997 set out the main elements of the so-called Washington Consensus. These included, but were not limited to such concepts as financial markets operating on a partially liberalized basis, competitive exchange rates, tariffication of import quotas, removal of barriers to entry impeding foreign firms, equal terms of competition between foreign and domestic firms, privatization of state owned enterprises, the removal of government regulations which do not aim at improving personal safety, protection of the environment or prudential soundness of financial markets, and the protection of property rights.[8]

The intellectual pedigree of this approach, at least in the United States of the 20th Century, can arguably be traced back to a number of influential economists from the Chicago School, the best known of which was probably Milton Friedman.[9] Friedman, in a career spanning several decades, consistently advocated in favor of a number of core free-market principles, many of which were elucidated in his 1962 publication "Capitalism and Freedom".[10] Friedman himself summarized the major theme of his treatise as "the role of competitive capitalism - the organization of the bulk of economic activity through private enterprise operating in a free market - as a system of economic freedom and a necessary condition for political freedom."[11]

Although the degree of orthodoxy with which countries tend to follow such a free-market approach varies enormously, there are a significant number of nations that - generally speaking - organize the bulk of economic activity within their respective territories along these lines and this number has undoubtedly been on the rise since the end of the Cold War. Nevertheless, in many countries, both developed and developing, governments choose to intervene into various sectors of the economy, for different policy reasons and to differing degrees; something that will be discussed below under section 3 of this Part.

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6 By way of example, one commentator, in summarizing Nehru's economic ideas, notes that they included an affirmation that "[d]eveloping societies should be based on collective action rather than on the acquisitiveness of capitalist society"; as well as the conviction that "[t]he State should seize control of the economy and induce all citizens to participate in the effort". Waelbroeck (1998) at p. 325.

7 Boughton (2004) at p. 18.

8 As summarized in Waelbroeck (1998) at p. 340.

9 Of course, Friedman's views, and those of the Chicago School more generally, could arguably be said to find their pedigree among such liberal thinkers as John Locke, Adam Smith, and John Stuart Mill, all of whom emphasized the importance of property rights, while at the same time advocating that government's role be limited to the "facilitation and adjudication of civil society" Yergin and Stanislaw (2002) at p. xiv.

10 See bibliography for more details.

11 Friedman (1962) at p. 4.

2. Authoritarian Capitalism

The label of authoritarian capitalism used here is synonymous with others, such as "illiberal capitalism"[12], "state-directed capitalism"[13], "state capitalism"[14], or "command-and-control capitalism"[15]. All of these terms seek to capture the essence of an economic system where the state has recognized the supremacy of markets over central planning, but has not shown a willingness to allow market forces to be the primary determinant of economic activity. This "new"[16] form of economic governance has captured the attention of many observers in the West, and has come to be viewed with varying levels of mistrust and skepticism.[17]

Regardless of how one may be disposed towards such state-directed manifestations of market-based economic governance, the point of the present analysis is to describe some of the ways in which the State has ventured into markets, and to arrive at some kind of typology that might be helpful as we examine ways in which multilateral constraints on these kinds of interventions have operated in the past and are emerging in the present.

One typology which may be helpful is that of a limited number of resource-rich countries who depend heavily on either oil or other mineral-based natural resource endowments, in which the state plays a disproportionately large role in the economy by virtue of its ownership of these resources. Such states would include Russia, Venezuela, as well as many of the Gulf States. [18]

Another typology would be that of a sub-set of countries that have prospered largely thanks to an export-led industrialization strategy where the State was the only entity with deep enough pockets to provide the initial capital required for national champions to emerge and be able to compete on export markets and where the State also played an important role by rigging the playing field decisively against foreign competition. This would apply to most of East Asia but for our purposes includes China, Chinese Taipei, Korea, Malaysia, Thailand and to a more limited extent Singapore.[19] The degree to which these economies can still be characterized as being subject to state-led capitalism varies, but for diverse reasons - most of which coincide strongly with the concentration of economic power among political elites - the influence the State exercises on the overall direction of the economy can be deemed well in excess of many if not most liberal democracies organized along the lines of market capitalism.

Another aspect of the analysis here is how the state opts - under state-led capitalism - as a matter of policy choice, to intervene in the economy and thereby influence market outcomes. One such way, already alluded to above is by ownership of the resources that dominate a country's economy. Thus, state ownership is highly prevalent in the oil and gas sectors, but also in industries as diverse as power generation, the production of iron and steel, port management, maritime shipping, armaments manufacturing, industrial machinery, telecommunications and civil aviation.[20] Another way in which the state has seen fit to intervene in markets, and the subject of significant controversy since the

[12] See for example Rachman (2008).
[13] This term is used for example by Halper (2010) at p. 104.
[14] See for example Bremmer (2009).
[15] This term is also used by Halper (2010) at p. 122.
[16] Many economic historians have argued very convincingly that there is nothing really "new" about this form of economic governance and that if anything, free market capitalism is the more recent arrival; see for example Chang (2008).
[17] See for example Wolf (2007).
[18] See Halper (2010) at p. 68.
[19] See Felipe (2003) at p. 4 (footnote 7).
[20] These examples provided by Halper (2010) at p. 122.

global financial crisis, is by establishing sovereign wealth funds (dealt with in more detail below under chapter III).

Finally, *The Economist*, in a recent article documenting in some detail the involvement of the state in the Chinese economy[21], set out what it refers to as a "taxonomy of privatization". In doing so, it essentially describes four categories of corporate entity operating on the Chinese market subject to varying degrees of state direction or support. The first of these categories is made up of what *The Economist* refers to as "large state-controlled enterprises", comprising "vast banks and transport, energy and telecoms providers that were, and to some extent still are, government ministries."[22] The second category in *The Economist*'s analysis comprises "joint ventures between private (often foreign) companies and firms backed by the state".[23] The third category is populated by "companies that are largely in private rather than state ownership, but in which the state remains influential nevertheless".[24]The fourth category of company identified by *The Economist*, is a more recent addition to the Chinese corporate landscape, and comprises those entities where the "state plays the role of a venture capitalist: local governments invest in or create funds that back companies that they hope will bring both jobs and financial returns".[25]

3. Relevant Degrees of State Intervention for the Purposes of this Paper

The degree to which a government opts to become involved in markets is ultimately a question each State must determine for itself in line with the national economic interest as it perceives it. Like so many other areas of government activity, this issue is ultimately a matter of State sovereignty. N. Gregory Mankiw in his seminal work "Principles of Economics", points out that governments essentially have two over-arching policy rationales for intervening in markets, the one is to promote efficiency, the other is to promote equity.[26]

Alan Deardorff goes slightly further and describes three categories of policy rationale for governments to intervene in markets: "correction of market failures (distortions, this would fit under the promotion of efficiency in Mankiw's framework); redistribution of income (promotion of equity); and non-economic objectives."[27] In addition to these three categories, Deardorff lists a fourth category, which he refers to as "intervention-induced intervention" (another variation of Mankiw's promotion of efficiency theme).[28] Redistribution of income is an obvious enough policy rationale - achieved largely by means of the tax system and, among others, various welfare programs. As examples of non-economic objectives, Deardorff lists national security and promoting cultural identity. A discussion of market failures and "intervention-induced intervention" as described by Deardorff is provided below in slightly more detail and specifically in the context of the kind of interventions typically identified under various models of state-led capitalism.

Market failure is generally described as manifesting itself in one of several forms. In general, it tends to be defined as a situation in which, left to themselves, market forces fail to efficiently allocate resources.[29] One such form of market failure is information asymmetries, where different market participants, particularly buyers and sellers, have vastly different levels of information on the quality

[21] "Capitalism Confined" September 3, 2011.
[22] *Ibid*.
[23] *Ibid*.
[24] *Ibid*.
[25] *Ibid*.
[26] Mankiw (2011) at p. 12.
[27] Deardorff (2000) at p. 73.
[28] *Ibid*, at pp. 78 *et seq*.
[29] Mankiw (2011) at p. 12.

(and thus the value) of the goods and services being sold or with regard to other market conditions.[30] Another form of market failure is negative externalities, where the actions of one set of economic actors have negative effects which are incurred by another set of participants. The most commonly cited example of this kind of market failure is pollution. Yet a third kind of commonly recognized market failure is the concentration of market power in such a way that a single economic actor or small group of economic actors are able to alter market outcomes (normally by unilaterally setting prices) in their favor.

Governments intervene in various ways to correct such market failures. For example, in order to combat information asymmetries they take measures to bring about greater transparency, or increases the degree of consumer protection by allowing consumers to unilaterally withdraw from some contracts within a certain period. To combat negative externalities, they may try to put a price on carbon emissions or require those who produce pollution to alter their production methods and force them to produce in a more environmentally friendly way, or to produce goods in a way that does less harm to the environment. In order to combat the concentration of market power, governments enact and enforce competition laws, or they impose price controls on certain goods deemed to be essential items.

As alluded to above, Deardorff refers to other forms of state intervention, namely "intervention-induced intervention". According to Deardorff, such interventions are the result of previous interventions in the economy, and are intended to correct the unintended consequences of previous interventions. In Deardorff's own words, these are "cases of policy intervention that are motivated not by any underlying objective or distortions that would be present in the absence of government, but only by the distortions that have been introduced by other government policies."[31]

The kinds of state intervention addressed by this paper typically tend to go beyond those motivated by such policy considerations as increasing equity, correcting perceived market failures or even mitigating the unwanted effects of previous government interventions, although these policy rationales may certainly play a role in the original design or subsequent justification of the kinds of government interventions I seek to address here. Rather the kinds of interventions addressed are those where the State takes it upon itself to participate in a given market either as economic actor itself, or where it intervenes directly to tilt the playing field in favor of economic actors it either owns, controls or has some other interest in. The three examples we focus on in more detail here are State Trading Enterprises (STEs), Sovereign Wealth Funds (SWFs) and State-Owned Enterprises (SOEs). In discussing the emerging set of rules finding their way into international treaties or other multilateral frameworks, other forms of government intervention will become apparent.

[30] See Mankiw (2011) at p. 468 for a brief discussion of this although Mankiw does not identify information asymmetries as a form of market failure *per se*.

[31] Deardorff (2000) at p. 79.

II. MULTILATERAL DISCIPLINES ON STATE TRADING ENTERPRISES

State Trading Enterprises for the purpose of the present discussion are those which fall under the definition found on the WTO's website, namely "governmental and non-governmental enterprises, including marketing boards, which deal with goods for export and/or import".[32] More substance is lent to this description in the WTO Understanding on the Interpretation of Article XVII[33], which attempts to provide a working definition of the kinds of enterprises Member governments must provide regular notifications on:

> "Governmental and non-governmental enterprises, including marketing boards, which have been granted exclusive or special rights or privileges, including statutory or constitutional powers, in the exercise of which they influence, through their purchases or sales, the level or direction of imports or exports."[34]

In terms of the typology set out above, as will become more obvious in the discussion which ensues below, governments tend to establish and justify the continued existence of STEs in terms of both equity arguments (ensure sustainable livelihoods for agricultural producers and rural communities) and in response to what is commonly viewed as the "unique nature" of agricultural markets. The establishment of STEs might also be viewed as a manifestation of Deardorff's "intervention-induced intervention" rationale, since global agricultural markets, in addition to being characterized by price-instability, are also notoriously distorted (due to various and extensive government interventions on these markets). But STEs are often set up and run by agricultural producers themselves, with direct support from the State, and can thus be qualified as a market intervention whereby the State seeks to influence market outcomes in favor of a set of economic actors that it has an interest in, usually because it has been captured by them or because of their ability to influence electoral outcomes.

A. The Original GATT Rules

1. *The Rules under GATT 1947*

The original GATT rules on STEs served a number of policy objectives. On the one hand, they were originally conceived as an interface mechanism for free-market economies to be able to conduct trading relations with planned economies.[35] On the other hand, and in the end more importantly, they were also intended to serve as an anti-circumvention tool in order to reinforce commitments on tariff concessions and the abolition of quantitative restrictions.[36]

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32 See: http://www.wto.org/english/tratop_e/statra_e/statra_e.htm (November 22, 2011).

33 Note that the GATT rules on STEs and the relevant WTO Understanding are appended to this paper in Annex I.

34 As cited at: http://www.wto.org/english/tratop_e/statra_e/statrad.htm (November 22, 2011).

35 This was acknowledged as early as 1943 in the context of the Anglo-American discussions under Article VII of the Mutual-Aid Agreement between the United States and the United Kingdom, on Commercial Policy. Under the topic of state trading, these discussions found that "It is necessary […] that methods and arrangements for trading between private-enterprise countries and state-trading countries, whether bilateral or multilateral, be such as to take account of this situation in order that the interests of both may be harmonized." Cited in: Irwin, Mavroidis & Sykes, at p. 232.

36 It should be recalled that the GATT was essentially conceived as the commercial policy chapter of what was intended to become the charter of the International Trade Organization. Seen from this perspective, the key underlying purpose of the GATT was to shore-up and avoid the circumvention or undermining of the tariff concessions which had been granted at the same time it was enacted. Thus the rules on elimination of quantitative restrictions, those governing non-discrimination, transparency, freedom of transit and customs valuation, essentially served to prevent the balance of rights and obligations which the mutual exchange of tariff concessions was intended to achieve, from being nullified or impaired. Mavroidis qualifies the GATT as a "negative integration-type of contract" which is certainly another and equally valid way of viewing it; see Mavroidis (2005) at p. 278.

GATT Article XVII entitled “State Trading Enterprises” contains the bulk of the disciplines adopted in this context, but is supplemented by paragraph 4 of Article II on Tariff Concessions. These disciplines, although not outlawing or even heavily proscribing the use of STEs, do impose a number of obligations, the most important of which is to require that such entities observe the principle of non-discrimination, and that they make purchasing decisions based on commercial considerations. The GATT rules also impose some transparency obligations.

GATT Article XVII requires that each contracting party who establishes or maintains STEs, ensure that such enterprises, in the context of their purchases or sales involving imports or exports, “act in a manner consistent with the general principles of non-discriminatory treatment”.[37] The next paragraph of this provision goes on to provide additional guidance as to what the obligations set out in paragraph 1 (a) entail, namely that such enterprises “make any purchases or sales solely in accordance with commercial considerations, including price, quality, availability, marketability, transportation and other conditions”.[38] Finally, this paragraph requires that STEs, “afford the enterprises of the other contracting parties adequate opportunity, in accordance with customary business practice, to compete for participation in such purchases or sales”.[39]

Paragraph 2 of this article essentially contains a carve-out from the operation of its provisions, namely for government procurement. Thus STEs which buy goods for use by the State or public bodies are not required to observe the non-discrimination obligations that the article otherwise imposes, although this paragraph does contain fair and equitable treatment language, that can be considered largely non-actionable.

Given that one of the purposes of the General Agreement from the very outset was the expansion of world trade, paragraph 3 of this Article also contains language recognizing the seriously detrimental and trade-inhibiting effects that STEs could potentially have, as well as non-actionable language on the importance of being able to negotiate in order to “limit or reduce such obstacles” in future.[40]

GATT Article II, entitled “Schedule of Concessions” sets out the mechanism by which contracting parties exchange and establish tariff bindings, and it also provides the legal instrument which then makes the schedules on which such bindings are inscribed part of the General Agreement and thus part of the binding and actionable rights and obligations entered into under the General Agreement. Paragraph 4 of Article II contains anti-circumvention language, in the event that a contracting party might try to frustrate market access expectations created by the granting of a tariff concession on a product, by subsequently establishing a government monopoly for the importation of such product. The language contained in this article sets out that “such monopoly shall not […] operate so as to afford protection on the average in excess of the amount of protection provided for in that Schedule”.[41]

The original GATT contained a third paragraph to Article XI on the General Elimination of Quantitative Restrictions. The language contained therein, providing that the provisions in the General Agreement in Articles XI to XIV on quantitative restrictions also applied to STEs. The practical implications of this was that a government monopoly could not limit the quantity of goods imported or exported except as permitted in the case of other quantitative restrictions (i.e. under one of the exceptions to the general ban on quantitative restrictions).

Like paragraph 4 of Article II on tariff concessions, this rule was essentially an anti-circumvention measure, enacted to ensure that governments did not undermine the general ban on quantitative

[37] GATT Article XVII:1(a).
[38] GATT Article XVII:1(b).
[39] *Ibid*.
[40] GATT Article XVII:3.
[41] GATT Article II:4.

restrictions by simply administering them through STEs. In the 1954/55 Review Session (discussed in more detail immediately below), GATT contracting parties agreed to move paragraph 3 of Article XI into an interpretative note.[42] The Ad Note reads as follows:

> "Throughout Articles XI, XII, XIII, XIV and XVIII, the terms 'import restrictions' or 'export restrictions' include restrictions made effective through state trading operations".

2. *Attempts at Policing State Trading Enterprises under the GATT*

In the 1954-55 Review Session, working parties were set up to discuss the operation of various GATT rules. Sub-Group III-B, which was discussing STEs, considered various proposals for amending the rules as they then stood on State trading, including the adoption of Articles 29-31 of the Havana Charter. However, the Working Party opted to essentially retain the existing structure of the Agreement in this context, and to add the current paragraph 4 of Article XVII (see below).[43]

Paragraph 4 of GATT Article XVII, adopted as a result of the 1954-55 Review Session, essentially contains several notification and information sharing obligations in the event that a contracting party has any commodities it imports or exports by means of STEs. It also required contracting parties operating an import monopoly of a product to provide information "at the request of another contracting party having a substantial trade in the product concerned" as to the mark up on the product, i.e. the difference between the landed price of the product and its onward sales price.

In 1957, a decision was enacted by the GATT to call for contracting parties to submit notifications under Article XVII.[44] The decision also stipulated what sort of information contracting parties should provide. Some 21 notifications were submitted as part of this process, which were examined by a panel established to review them.[45] The panel concluded that the information provided was often insufficient, and drafted a new questionnaire to be circulated amongst GATT contracting parties (the 1960 questionnaire).[46] However, the responses to the new questionnaire were also disappointing.[47]

The issue of STEs , and their distortive effects on trade flows, continued to resurface within the GATT, in various shapes and guises. This was especially the case in the context of efforts to document and tackle barriers to developing-country exports, carried out predominantly under the auspices of the so-called Committee II and Committee III frameworks. The impetus for establishing these committees had come from a 1958 report to the GATT contracting parties, entitled "Trends in International Trade", otherwise known as the Haberler Report, after Gottfried Haberler, Professor of Economics at Harvard University, who among others, authored the report. The Haberler Report was mandated to make findings on a number of issues, including the widespread use of protectionist instruments against agricultural imports, which at the time, was perpetrated primarily by means of non-tariff measures and thus was beyond the ambit of the liberalization being achieved through the exchange of mutual tariff concessions.[48]

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[42] See WTO, Analytical Index: Guide to GATT Law and Practice, Volume 1, 1995, at p. 354
[43] See GATT Doc. L/1014 (1959).
[44] See GATT Doc. L/760 (1957).
[45] See GATT Doc. L/970 (1959), at p. 5.
[46] *Ibid*.
[47] See Jackson (1969), at p. 353.

Although the Haberler Report did not result in much tangible progress being made on liberalization of trade in agricultural products, one of the results commonly attributed to it was the establishment, shortly after the report was circulated, of three committees. Committee I began preparatory work for a new round of trade negotiations, which ultimately culminated in the Dillon and Kennedy Rounds.[49] Committee II focused on trade in agricultural products and revealed, in hitherto untold detail, the degree to which agricultural products were subject to protection by various non-tariff measures. Committee III, dealt with the exports of less developed countries. One of the findings of a 1961 report by Committee II was that the use, by some contracting parties of STEs had similarly prohibitive effects on trade as quantitative restrictions[50].

One of the more relevant results of the work undertaken in the GATT in the context of STEs during this period, was the development, by the Panel on Subsidies and State Trading, of a new questionnaire for contracting parties to provide notifications concerning the operation of STEs, in compliance with the obligations which resulted from the adoption of paragraph 4 of GATT Article XVII following the 1954-55 Review Session.[51]

The incidence of STEs, and the impact they had on trade also became well documented in the context of the so-called inventory of non-tariff measures, which was undertaken in the years immediately following the end of the Kennedy Round (1967-69), in preparation for the launch of the Tokyo Round. It was in the context of preparing for a future round of trade negotiations that GATT contracting parties mandated the GATT secretariat to draw up an inventory of non-tariff measures affecting trade between them.[52] The creation of the inventory was undertaken on the basis of notifications made by GATT contracting parties. After about two years, the secretariat had drawn up a list of some 800 notifications, and organized them into five categories, namely[53]: 1) government participation in trade (primarily through STEs); 2) customs and administrative entry procedures; 3) standards involving imports and domestic goods; 4) specific limitations on imports and exports such as QRs; and 5) restraints on imports and exports using pricing mechanisms.

Despite their inclusion in the NTM inventory, STEs were not the subject of intensive negotiations in the Tokyo Round. The negotiating group established to discuss nontariff measures had five subgroups, none of which was exclusively focused on the problems of STEs.[54] The Tokyo Declaration of September 1973 which launched the Round was also silent on STEs, although it did contain general language on such issues as “a substantial improvement in the conditions of access for the products of interest to the developing countries” as well as the desire to “reduce or eliminate non-tariff measures or, where this is not appropriate, to reduce or eliminate their trade restricting or distorting effects, and to bring such measures under more effective international disciplines”.[55] In fact, it was not until the advent of the Uruguay Round that STEs were to be addressed in any substantive manner.

3. *Dispute Settlement on State Trading Enterprises under the GATT*

Unlike the GATT provisions on non-discrimination and quantitative restrictions, the obligations GATT contracting parties entered into with regard to STEs were not extensively tested and interpreted within the context of dispute settlement during the GATT years. There does not seem to be any

49 Josling, Tangermann and Warley (1996), p. 38.
50 BISD, 9th Supplement, p. 110.
51 See L/970, Report by the Panel on Subsidies and State Trading Enterprises,
52 Winham (1986), p. 84.
53 *Ibid*, p. 87.
54 The five subgroups were (i) Quantitative Restrictions; (ii) Technical Barriers to Trade; (iii) Customs Matters; (iv) Subsidies and Countervailing Duties (v) Government Procurement [added in 1976 only]. See: Winham (1986), p. 100.
55 See Declaration Issued at the End of the Ministerial Meeting Held in Tokyo, 12-14 September 1973, reprinted in Winham (1986) at pp. 413 *et seq*.

consensus on why this was the case among scholars and observers. However, it is safe to say that, like the transparency obligations contained in GATT Article X, the obligations on STEs were almost 'auxiliary' in nature, meaning they were enacted in order to shore up and reinforce other, more actionable obligations, such as tariff bindings, the ban on quantitative restrictions, and non-discrimination obligations. Thus, if a measure was challenged under GATT Article XVII it was also inevitably challenged under either GATT Article XI (on quantitative restrictions), or on GATT Article I (MFN). A violation of GATT Article XVII was thus generally raised in the alternative or in addition to a complaint of a violation of another obligation.

This was the case in the 1988 dispute *Japan – Trade in Semi-conductors*, in which the Canadian government (also a party to the dispute, alongside the EC), claimed that the semiconductor agreement between the United States and Japan, violated GATT Article I (MFN) as well as Article XVII.1 (c), which enjoins contracting parties to refrain from preventing private companies under their jurisdiction from observing the principles of non-discrimination as set out in paragraph (a) and (b) of that article. Thus Article XVII was raised in connection with a violation of a principal GATT obligation (most favored nation treatment). The panel in this dispute dismissed the Canadian claim on the grounds that there was nothing inherently discriminatory about requiring companies to provide information in compliance with an export monitoring scheme (one of the actions required under the US-Japan semiconductor agreement).[56]

In coming to its conclusion in the Semiconductor case, the panel relied on case law which had been established under a 1984 dispute, *Canada – Administration of the Foreign Investment Review Act*. The FIRA dispute involved written undertakings made by investors when applying to invest in Canada under the Act, which was adopted in 1973 and entered into force the following year. These written undertakings either involved commitments to purchase from Canadian sources of supply, or a specific percentage of Canadian products or to favor Canadian products over imported ones. They also included undertakings to manufacture in Canada. Finally, the undertaking also involved export undertakings in a variety of forms.[57]

The United States, which was the source of more than fifty percent of the investment reviews carried out in application of the FIRA, initiated a case under the GATT in January 1982. It challenged the manner in which the Act was being administered, since the Act itself did not explicitly require any of the undertakings discussed above. The US challenged the purchase, manufacturing and export undertakings under a number of GATT provisions, including Articles III:4 and III:5 (national treatment), XI (prohibition on quantitative restrictions) and under the rules on STEs, namely Article XVII (c).[58]

In the context of its Article XVII (c) complaint, the US argued that the purchase undertakings prevented investors "from acting solely in accordance with commercial considerations" thus violating Canada's obligations under this provision.[59] It made similar arguments against the exporting undertakings.[60] The Panel examined the language of Article XVII and the corresponding negotiating history from the ITO Charter which had been examined in depth by the Canadian defense. Although the Panel essentially exercised what today would be characterized as judicial economy, by declining to rule on the substance of this question, because it had already ruled that the purchase undertakings were inconsistent with GATT Article III:4 (national treatment), it also made one finding in this context which was significant, and which was later relied upon by the *Japan – Semiconductors* Panel already

[56] See *Japan – Trade in Semi-conductors*, Report of the Panel adopted on 4 May 1988, at paragraph 80, available at: http://www.worldtradelaw.net/reports/gattpanels/japansemiconductor.pdf (November 22, 2011).
[57] See *Canada – Administration of the Foreign Investment Review Act*, Report of the Panel adopted on 7 February 1984, at paragraphs 2.5 f., available at: http://www.worldtradelaw.net/reports/gattpanels/canadafira.pdf, (November 22, 2011)
[58] *Ibid*, at paragraphs 3.1 *et seq*.
[59] *Ibid*, at paragraph 3.14.
[60] *Ibid*, at paragraph 3.20.

discussed above. This finding essentially held that the commercial considerations criterion only becomes relevant "after it has been determined that the governmental action at issue falls within the scope of the general principles of non-discriminatory treatment prescribed by the General Agreement".[61]

By this the Panel presumably meant that only once it has been found that the governmental action or measure at issue constitutes a violation of one of the General Agreement's non-discrimination obligations could a Panel proceed to examine whether there had also been a violation of the "commercial considerations" language under GATT Article XVII (c). Strangely enough, this is what the Panel did in this case, in the sense that it first determined that the governmental action in question violated GATT Article III:4. However after having done so, it claimed that it was no longer required to make any explicit findings on "commercial considerations". This contradiction seems not to have been apparent to the Panel, or perhaps was not pointed out to them.

Apart from the Japan Semiconductors case and the FIRA dispute, STEs as an issue seem to have gone all but unnoticed during the GATT years, at least in terms of dispute settlement. Even after the Uruguay Round and the establishment of the WTO, the issue of STEs has, as we shall see below, not been heavily contested in the context of dispute settlement. What limited developments have occurred, have generally taken place in the context of the Working Party, also discussed below.

B. The Prevailing Framework under the WTO

1. The Uruguay Round and State Trading Enterprises

As mentioned above, early efforts to deepen the understanding of GATT contracting parties on the prevalence, operation and impact of STEs, by means of notification obligations, only yielded limited success. Efforts to improve the quality and frequency of notifications following the end of the Tokyo Round met with some initially encouraging signs, but then faltered.[62] One of the reasons commonly cited for the poor quality of notifications as well as the lack of enthusiasm by contracting parties to provide notifications on this area of activity was the fact that there was still a great deal of ambiguity about what kinds of enterprises were subject to the notification obligations.[63] This led GATT contracting parties, particularly those most concerned about the trade-distorting effects of such enterprises, to seek to improve the existing disciplines on State trading in the course of the Uruguay Round. These efforts ultimately led to the adoption of the Understanding on Interpretation of Article XVII.

The Punta del Este Declaration which formally launched the Uruguay Round, like that which had launched the Tokyo Round some thirteen years before it, was completely silent on the issue of STEs. The Declaration did however contain a mandate to "review existing GATT Articles, provisions and disciplines" and moreover, one of the primary objectives of the negotiations was the "improvement of access to markets by the reduction and elimination of tariffs, quantitative restrictions and other non-tariff measures and obstacles".[64]

61 *Ibid*, at paragraph 5.16.

62 A study on state trading enterprises was carried out in 1995 by the US General Accounting Office, covering the period between 1980 (the year the results of the Tokyo Round were implemented) and 1994 (the year the results of the Uruguay Round were adopted). According to the GAO's study, 1981 was the best year for compliance with the notification obligations under Article XVII.4, however even in 1981, some 79 percent of GATT contracting parties failed to make any notifications at all on STEs; see GAO (1995), at p. 6.

63 *Ibid*.

64 See Ministerial Declaration on the Uruguay Round, contained in GATT/ 1396 of 25 September 1986, available at http://gatt.stanford.edu/page/home (November 22, 2011).

The Punta del Este Declaration also contained very explicit language on bringing trade in agricultural products under "more operationally effective GATT rules and disciplines".[65] The negotiations on agriculture which ensued under the auspices of the Uruguay Round produced an Agreement on Agriculture that contained actionable language relevant for STEs in the context of both the obligation to convert non-tariff measures into ordinary customs duties,[66] and their possible use to circumvent export subsidy reduction commitments.[67]

Most of the negotiations on STEs during the Uruguay Round occurred under the auspices of the "GATT Articles" negotiating group (the mandate being to "review existing GATT Articles, provisions and disciplines"). This group also discussed tariff schedules, renegotiation of tariff concessions, regional agreements, waivers, non-application of the GATT, balance of payment articles and the so-called "grandfather clause" of the Protocol of Provisional Application.[68]

Although some GATT contracting parties were in favor of amending the substantive aspects of the rules governing STEs, this was not a position that was able to gain much traction as the Uruguay Round progressed. The only proposed changes that enjoyed a suitable degree of consensus were on clarifying the notification obligations, creating counter-notification procedures and the establishment of a regular mechanism for discussing such notifications as well as any problems which arose in the context of STEs.[69]

Although the Round itself lasted from September 20, 1986 to December 15, 1993, negotiations on STEs were for all intents and purposes concluded by 1990[70], meaning that these talks were predominantly technical in nature, and were largely devoid of the highly politicized negotiating compromises and trade-offs which otherwise characterized the agriculture negotiations, especially on such issues as tariffication, binding limits on domestic support outlays and the effective banning of export subsidies unless they had been scheduled (with mandatory reductions to the use of scheduled export subsidies).

For all intents and purposes, the results of the Uruguay Round negotiations on state trading enterprises (apart from the related provisions of the Agreement on Agriculture already referred to above), are contained in the Understanding on the Interpretation of Article XVII of the General Agreement on Tariffs and Trade 1994.[71] The Understanding requires Members to review their own policies in the area of STEs, taking into consideration the definition provided therein, and to make notifications accordingly, using the 1960 questionnaire.[72] The Understanding also provides a counter-notification mechanism[73], and establishes a Working Party under the Council for Trade in Goods, to review and discuss the notifications received.[74] Below we examine in more details the activities of the Working Party on State Trading Enterprises since the WTO came into force, but first we examine how the issue of STEs has been handled in the context of WTO dispute settlement.

65 *Ibid*.
66 This was known as "tariffication" and was set out in Art. 4.2 of the Agreement on Agriculture.
67 Art. 10, Agreement on Agriculture.
68 See Croome (1995) at pp. 216 et seq.
69 *Ibid*, pp. 97 and 217.
70 See GAO (1995) at p. 11.
71 For ease of reference, I provide this definition again here: "Governmental and non-governmental enterprises, including marketing boards, which have been granted exclusive or special rights or privileges, including statutory or constitutional powers, in the exercise of which they influence through their purchases or sales the level or direction of imports or exports".
72 WTO Understanding on the Interpretation of Article XVII, paragraphs 2 and 3.
73 *Ibid*, para. 4.
74 *Ibid*, para. 5.

2. *WTO Dispute Settlement and State Trading Enterprises*

The cases which have perhaps done the most to shine a spotlight on the operation and potential abuses of STEs by WTO Members are the two complaints brought by the United States and Australia respectively against Korea regarding restrictions on the importation of beef[75], as well as the complaint brought by the United States regarding wheat exports and the treatment of imported grain.[76]

In *Korea-Beef*, the dispute essentially revolved around the actions of Korea's Livestock Products Marketing Organization (LPMO), which operated an elaborate system for regulating beef imports on the basis of bilateral quotas negotiated with the complainants (and Canada, who was a third party to the dispute) during the course of the Uruguay Round, and in application of the Korean Government's Management Guideline for Imported Beef. The STE in question, the LPMO, was established in 1988 and had been exclusively authorized to administer beef imports. The LPMO itself imported a large, albeit diminishing share of the beef quota, but in any event authorized and distributed quota allocations for any beef not directly imported by it.[77] The complainants in these cases, which were heard before the same panel, focused on a number of alleged violations, the most important of which were national treatment violations under GATT Art. III and breaches of Korea's domestic support commitments under the Agreement on Agriculture. However, the Panel report contained some lengthy deliberations on the "provisions and jurisprudence on restrictions imposed by state-trading enterprises".[78] Ultimately, the panel found that due to the actions of the LPMO, particularly restrictions placed by it on the distribution of imported beef which inevitably affected its import decisions, the LPMO and thus Korea had failed to act in a manner consistent with the general principles of non-discriminatory treatment, as required under GATT Art. XVII:1(a).[79] These findings were not the subject of appeal and thus were neither upheld nor reversed by the Appellate Body. Nor were they the real matter at issue in the case, but rather secondary arguments to the complaints under GATT Articles II and III and those based on Art. 4.2 (tariffication) and Articles 3, 6 and 7 (domestic support commitments) of the Agreement on Agriculture.

In *Canada-Wheat*, the United States brought a number of claims, most of which involved Art. III national treatment issues. However, part of its claim was directed against the Canadian Wheat Board (CWB) and its alleged breach of Canada's obligations under GATT Art. XVII on STEs. The panel deliberated at great length on the export operations of the CWB, and claims by the United States that these exports failed to meet the "commercial considerations" language contained in GATT Art. XVII:1(b).[80] The panel ultimately found that the United States had failed to demonstrate that the export sales made by the CWB were on non-commercial terms, and that as a result, it had failed to establish a breach, by Canada, of its obligations under GATT Art. XVII:1.[81] Before arriving at this conclusion however, the panel made some noteworthy findings pertaining to STEs, including "if a Member's STE does not act in accordance with the principles of Article XVII:1(a) or (b), or if it is clear from relevant facts and circumstances that the STE will not so act, this *ipso facto* places the Member concerned in breach of the undertaking contained in Article XVII:1(a)."[82] The panel also clarified the meaning of the term "commercial considerations" in Article XVII:1(b), as implying that STEs "should seek to purchase or sell on terms which are economically advantageous for themselves and/or their owners, members, beneficiaries, etc."[83] The panel further elucidated on this definition by stating that

75 *Korea - Measures Affecting Imports of Fresh, Chilled and Frozen Beef* (DS 161/169).
76 *Canada - Measures Relating to Exports of Wheat and Treatment of Imported Grain (DS 276).*
77 Beef imports were also taking place by means of a Simultaneous Buy/Sell" ("SBS") system; see Report of the Panel, at paras. 8-29 (pp. 3 - 7).
78 Report of the Panel, at paras. 747-769 (pp. 174-179).
79 Report of the Panel at para. 769 (p. 179).
80 Report of the Panel at paras. 6.29 - 6.151 (pp. 141 - 169).
81 Report of the Panel at para. 6.151 (p. 169).
82 Report of the Panel at para. 6.42 (p. 144).
83 Report of the Panel at para. 6.87 (p. 154).

it held that an STE would not be acting solely in accordance with commercial considerations if it purchases or sells on the basis of "such considerations as the nationality of potential buyers or sellers, the policies pursued by their governments, or the national (economic or political) interest of the Member maintaining the STE."[84] However the panel also qualified its reasoning by noting that Article XVII:1(b), "does not require export STEs to make sales solely in accordance with 'fair' commercial considerations"[85] or for the purpose of maximizing profit, since they might also be used as an instrument to achieve such policies as enhancing food security, reducing alcohol consumption, or achieving price stabilization.[86]

To summarize, what little case law as has been handed down by the dispute settlement organs of the WTO on STEs would indicate that, in line with the relatively weak or "soft" nature of the obligations set forth in GATT Art. XVII, Members have been reluctant to rely on this language and this language alone in order to underpin their complaints while trying to establish nullification and impairment of benefits, and the dispute settlement organs have tended to oblige them in this view.[87] Rather, complaints have been based, and have generally tended to succeed on the basis of more actionable or "harder" obligations, such as non-discrimination, or, as was the case in Korea-Beef, the binding commitments Members entered into under the Agreement on Agriculture.

3. The WTO Working Party on State Trading Enterprises

The Working Party on State Trading Enterprises was established by the Council for Trade in Goods at its meeting on 20 February 1995, pursuant to paragraph 5 of the Understanding on the Interpretation of Article XVII of the General Agreement on Tariffs and Trade 1994. It was mandated to do essentially three things under paragraph 5 of the Understanding, namely (1) review notifications and counter-notifications; (2) review the adequacy of the 1960 questionnaire on the basis of the notifications received; and (3) develop an illustrative list showing the kinds of relationships between governments and enterprises, and the kinds of activities, engaged in by these enterprises, which may be relevant for the purposes of Article XVII.

In the early years of the WTO the Working Party was kept relatively busy attending to this mandate, meeting as many as 10 times in 1997, although since then, the frequency of meetings was considerably less.[88] After some initial difficulties on achieving consensus on such issues as the type of statistical information to be requested in the questionnaire, a revised questionnaire on State-trading (G/STR/3) was finally agreed on and adopted at its meeting of 2 April 1998.[89] Similar difficulties initially slowed work on elaborating an illustrative list, with the specific problem in this context being reaching an understanding on what constituted an exclusive or special right or privilege in the sense of Article XVII and the Understanding. Nevertheless The Illustrative List (G/STR/4)[90] was approved at the Working Party's meeting of July 1999 and was subsequently adopted by the Council for Trade in Goods at its meeting of 15 October 1999.

[84] Report of the Panel at para. 6.88 (p. 154).
[85] Report of the Panel at para. 6.101(p. 157).
[86] Report of the Panel at para. 6.96(p. 156).
[87] As seen by the Panel's reluctance in *Canada-Wheat* to interpret the language of GATT XVII:1(b) as broadly and stringently as the US would have it do, a finding that was upheld by the Appellate Body on appeal.
[88] The Working Party on State Trading Enterprises in general only meets once or twice a year in formal session and may meet once or twice in informal consultations. In 2005, it did not meet at all due to preparations for the sixth Ministerial Conference which took place from 13–18 December in Hong Kong.
[89] The Council for Trade in Goods approved the revised questionnaire at its meeting of 21 April 1998; see Report (1998) of the Working Party on State Trading Enterprises (G/L/281) dated 26 November 1998.
[90] The full title of the document is Illustrative List of Relationships between Governments and State Trading Enterprises and the Kinds of Activities Engaged in by these Enterprises.

The Working Party has arguably proven less successful in accomplishing the first of the three mandates entrusted to it by Members under the Understanding, namely to review notifications by Members. Some Members have submitted notifications and these have been reviewed, in fact many of the biggest users of STEs have duly submitted notifications in one form or another, at one time or another. However the main challenge of the Working Party since it first took up its mandate and until today, continues to be improving the rate of compliance by WTO Members with the duty to notify. The 2011 Annual Report of the Working Party notes in this respect that "as of 27 October 2011, 28 notifications (out of a possible 126 notifications) have been received for the 2010 notification period […] and 38 notifications (out of a possible 126 notifications) for the 2008 notification period. The rate of compliance can thus be qualified as very low. This is a problem that has been addressed in every formal meeting of the Working Party, but up to now, no practical and effective solution has been found. Many Members simply lack the technical expertise, manpower, policy imperative or political will to complete and submit a questionnaire on the STEs operating in their economies. Others simply submit a one-page notification announcing that there are none.[91]

4. State Trading Enterprises and the Doha Development Agenda

There is no mention of the STEs in the Ministerial Declaration that launched the Doha Round. The language in the Declaration pertaining to "Agriculture" (where STEs are most prevalent) focuses on the traditional three pillars of market access (improving it), export subsidies (eliminating them) and trade-distorting domestic support (reducing it substantially). The section of the Declaration which addresses "WTO Rules", of which GATT Art. XVII has traditionally been considered a part[92] also focuses on the rules on antidumping and on subsidies and countervailing measures (including fisheries subsidies), as well as on regional trade agreements. This despite the fact that, in the years immediately preceding the Round, some countries submitted negotiating proposals that also included suggestions for new disciplines on STEs.[93]

As the Round has progressed however, the collective thinking of Members seems to have coalesced around the idea that STEs are primarily a problem in the context of helping countries obtain a disproportionate share of the world market in certain agricultural exports. Thus they have largely been treated in the context of anti-circumvention rules on achieving the eventual elimination of agricultural export subsidies. Annex K of the Revised Draft Modalities for Agriculture of December 2008[94] entitled "Possible New Article 10bis of the Agreement on Agriculture: Agricultural Exporting State Trading Enterprises" sets out a number of proposed new disciplines aimed at constraining and eventually eliminating the privileges and monopolies of these entities by 2013. In fact, a reading of the language which seems to be emerging from the agriculture negotiations on STEs seems to mirror in many ways the arguments and concerns expressed by the United States in the Canada-Wheat case discussed above. Whereas the "softer" disciplines contained in GATT Art. XVII have proven ineffective in policing the worst abuses of STEs, the very hard disciplines on export subsidies are surely up to the task.

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91 For an example of this, see Nigeria's notification dated 27 April 2011 (G/STR/N/13/NGA), in which it proclaims "The Government of the Federal Republic of Nigeria wishes to notify the Working Party on State Trading that, in accordance with Article XVII:4(a) of GATT 1994, Nigeria no longer maintains any State trading entity as at 30 June 2010." For an economy as large and diverse as Nigeria, with a sizeable state-controlled energy sector, this statement seems highly unlikely to be completely accurate.

92 The WTO Rules Division has substantive responsibility for GATT Art. XVII.

93 MacLaren D. & McCorriston S. (2002), p. 131 *et seq*.

94 TN/AG/W/4/Rev.4

C. Economic Significance of STEs in Global Markets

MacLaren D. & McCorriston S. (2002) point out the importance of STEs on global agricultural export markets, noting that, for wheat, the Australian and Canadian Wheat Boards account for the entirety of these countries' exports of this commodity, and that together, these countries account for almost 30 percent of global wheat exports (Australia has since abolished the AWB's export monopoly, in 2008, and legislation to end the Canadian Wheat Board's single desk was before the Canadian Parliament at the time of writing).[95] Notifications to the WTO show that in both Japan and Korea, STEs account for 100 percent of these countries' rice imports, as well as almost all imports of such products (for Japan) of wheat and barley and (for Korea) meat (as discussed briefly above in the context of the *Korea-Beef* case). Ackerman (1998), notes that for the period 1994-1997, between one-third and one-half of global wheat imports were conducted by STEs.[96] Ackerman (1998) also notes that "STEs account for about half of world rice exports and nearly a third of rice imports", as well as pointing out that the "New Zealand Dairy Board, handles about 30 percent of world dairy product exports" (the Board has since been absorbed into Fonterra, which was formed in 2001)[97]

Even today, a cursory look at the USTR's 2011 National Trade Estimate Report on Foreign Trade Barriers shows that STEs are considered an important impediment to a number of US exports. The Report notes that "[the] United States has longstanding concerns about the monopolistic marketing practices of the Canadian Wheat Board."[98] The report also cites concerns regarding the operation of STEs in China for petroleum and sugar imports[99], in India, for exports of high grade iron ore[100], in Indonesia, for rice imports[101], in Japan, for wheat imports[102], in Venezuela for a whole range of commodities deemed by the government to be basic foodstuffs[103], and in Vietnam for several residual items for which a phase-out period was agreed under Vietnam's protocol of accession.[104]

In light of the very poor record WTO Members have shown in complying with their notification obligations (as discussed above), one can only assume that the STEs discussed by academics such as MacLaren D. & McCorriston, or policymakers such as Ackerman and which find their way into the USTR's National Trade Estimate Report really only include the most obvious incidences of this policy instrument and those that have effectively been notified or otherwise documented (say in the course of a country's WTO accession working party report or trade policy review). In some commodities as we have seen and in others which we have not (such as energy) the incidence of STEs can safely be presumed to range anywhere from very high to all-pervasive.

D. Success of GATT/WTO Rules on Constraining State Trading Enterprises

It is probably safe to say that GATT disciplines aimed at constraining the proliferation and trade-restrictive effects of STEs have been weak and have largely failed to curb the damaging incidence of these enterprises in some of the least traded commodities like dairy products and rice. In the case of other commodities, most notably wheat, the grip of STEs seems to be relaxing slowly, although these entities still manage an important share of global trade in this commodity.

95 MacLaren D. & McCorriston S. (2002), p. 137.
96 Ackerman (1998), p. 43.
97 *Ibid*, p. 44.
98 USTR (2011), p. 52.
99 *Ibid*, p. 61.
100 *Ibid*, p. 182.
101 *Ibid*, p. 186.
102 *Ibid*, p. 196.
103 *Ibid*, p. 372.
104 These products include cigars and cigarettes, crude oil, newspapers, journals and periodicals, and recorded media for sound or pictures; Ibid, p. 379.

The reasons for this failure are easy enough to identify. The original GATT disciplines on these entities were of a minimalist nature and couched in language that was intended to be barely actionable. Moreover, STEs emerged to dominate the trade in commodities grown by a small number of highly-organized and disproportionally influential interest groups that, over time, became increasingly entrenched and immovable as a political force. Or they emerged to dominate the trade in commodities of obvious strategic importance to governments, like iron-ore and petroleum.

The prospects for reform on this particular front seem dim, since STEs have not been specifically addressed in the context of the - now almost defunct - Doha Round, except, as noted, where they are perceived to be a part of the broader problem of export competition, and largely seem to have fallen off the radar of policymakers all together.

III. A TENTATIVE FRAMEWORK ON SOVEREIGN WEALTH FUNDS

The US Treasury seems to qualify SWFs as any "government investment vehicle which is funded by foreign exchange assets, and which manages those assets separately from official reserves."[105] The International Working Group on Sovereign Wealth Funds (IWG, discussed below) itself defines SWFs as "special purpose investment funds or arrangements that are owned by the general government"[106], whereby it goes on to exclude from this definition "foreign currency reserve assets held by monetary authorities for the traditional balance of payments or monetary policy purposes, state-owned enterprises (SOEs) in the traditional sense, government-employee pension funds, or assets managed for the benefit of individuals."[107]

The first SWF is generally held to be the Kuwait Investment Board, set up in 1953.[108] Balin (2009) attributes what he refers to as the "next wave" of SWF creation to the "oil boom" of the 1970s (e.g. Abu Dhabi, Alaska and Alberta).[109] The most recent wave of SWF creation seems to be the result of both the most recent, prolonged increases in the prices of oil and other natural resources (Russia, Chile), as well as the buildup of foreign exchange reserves among a number of countries who have run persistent trade surpluses with the rest of the world (South Korea, China, Taiwan).

More in-depth analysis is provided below on the impact and importance SWFs have had on global investment and international financial markets, but for now it is helpful to point out firstly, in terms of their size as a group of investors, that estimates range from between 1.5 to 3 trillion dollars under management by SWFs[110]; and secondly that their investment activities have tended, as a group, to eschew politically sensitive sectors such as technology or other potentially strategic assets, and have instead been geared more towards a mixture of equities, bonds and "other forms of investment, including private equity, real estate, and commodities".[111]

The aggregate size of the funds under management by SWFs dwarfs that of transfers made under the auspices of official development aid, but is itself tiny compared to the size of privately held investments across global financial markets.[112] Nevertheless, SWFs probably started to appear on the radar screen of central bank officials and other policymakers concerned with the stability of the international financial system sometime between March 2007 and April 2008. This was the period during which, owing to their increasingly dire balance-sheet situation in light of exposure to a rapidly deteriorating US mortgage market, Citigroup, Merrill Lynch, and Morgan Stanley received an estimated USD 31 billion from SWFs owned by the governments of Abu Dhabi, Singapore, Kuwait, Korea, and China.[113]

The perceived rapid emergence of a group of state-directed and state owned financial titans was greeted with a certain degree of suspicion in some quarters.[114] This inevitably led to calls for SWFs to adhere to greater transparency and adopt established principles of sound corporate governance. The

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105 Clay Lowery, Acting Treasury Under Secretary for International Affairs, during his address "Remarks on Sovereign Wealth Funds and the International Financial System" on June 21, 2007 in San Francisco, as cited in Balin (2009), at p. 2.

106 IWG (2008), at p. 3.

107 *Ibid*, footnote 6.

108 Wong (2009) at p. 1081.

109 Balin (2009), at p. 2.

110 Mostrous, Gue & Dittman (2011), at p. 29.

111 See Balin (2009), at p. 6.

112 This assertion comes from Balin, who estimates the aggregate value of funds under management by SWFs at USD 3 trillion, and thus at the higher end of the scale; see Balin (2009), at p. 3.

113 Mostrous, Gue & Dittman (2011), at p. 35.

114 See, for example, the statements of Lawrence Summers and Senator Charles E. Schumer cited in Mostrous, Gue & Dittman (2011), at pp. 35 and 26 respectively.

response to these calls was the establishment of the International Working Group on Sovereign Wealth Funds in April/May 2008, discussed in greater detail below.

In terms of their place in the typology of state interventions set out at the beginning of this paper, SWFs set up by both oil or natural resource exporting countries as well as those countries who have amassed large foreign currency reserves as a result of persistent trade surpluses, would seem to be a policy response to the potential negative externalities commonly summed up under the term "Dutch Disease".[115] In this sense, SWFs represent an affirmative response to a massive accumulation of funds that could have a destabilizing effect on the real economy. In another sense, SWFs represent revenue-maximization strategies pursuant to which governments attempt to attain the greatest return, over the long term, for assets which they have become stewards of.

A. Potential Impact of SWFs on International Financial Markets

Beck and Fidora (2008) attempt to examine the impact of SWFs on both global capital flows, as well as exchange rates and asset prices but concede that it is probably too early to tell with any certainty what these might be, and that these impacts will in any event be contingent on the investment strategies pursued by SWFs.[116]By means of some very basic modeling and what they refer to as "back of the envelope calculations" they predict some outflows from the traditional US dollar and Euro denominated bonds (only partially offset by inflows into US and Euro denominated equities) into developing markets, as SWFs invest in emerging markets by means of long-term strategies that are sufficiently hedged so as to allow them to ride out the ups and downs of short-term market or political instability.[117] The upshot of this is that global investment flows may become significantly more diversified and by implication more systemically stable. With regard to the potential impact of SWFs on asset prices and exchange rates, Beck and Fidora note that "SWFs could have an impact on asset prices and exchange rates through price pressures or a change in risk aversion".[118]

Research performed by the IMF also seems to vindicate the findings of Beck and Fidora[119] while also noting that it failed to find any significant destabilizing effect of SWFs on equity markets.[120] Most studies seem to cite the uncertainty created by the underlying lack of transparency with which most SWFs tend to operate, a complaint that the Santiago Principles (discussed below) were explicitly intended to address.[121] In light of the fact that the size of the assets managed by SWFs is likely to continue growing, and given the efforts undertaken by SWFs to increase the transparency of their investments and to reassure the world that these are driven primarily by commercial considerations, the most probable scenario for their future impact is a continued and sustained diffusion of risk away

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115 Thus the SWF is established as a preventive measure by means of which the amassed funds are deployed without the inflationary and exchange-rate appreciation effects that would inevitably ensue if they were allowed or required to be converted into domestic currency. Dutch Disease is defined as "the negative impact on an economy of anything that gives rise to a sharp inflow of foreign currency, such as the discovery of large oil reserves. The currency inflows lead to currency appreciation, making the country's other products less price competitive on the export market. It also leads to higher levels of cheap imports and can lead to deindustrialisation as industries apart from resource exploitation are moved to cheaper locations." Source: Financial Times Lexicon, http://lexicon.ft.com/Term?term=Dutch%20disease (January 27, 2012).

116 Meaning whether they invest on the basis of purely commercial or other (non-commercial) considerations, whether they pursue a return or liquidity-based investment strategy, how much risk they are willing to take on and other factors.

117 Beck and Fidora (2008), pp. 14 *et seq*.

118 Ibid, p. 18.

119 See in particular the IMF Research Bulletin of March 2009, p. 4, available for download at http://www.imf.org/external/pubs/ft/irb/2009/01/index.pdf

120 Ibid.

121 See in particular Kotter and Ugur (2008).

from traditional bond and equity markets as well as continuing to be the equity injectors of last resort for troubled financial institutions as was so manifestly on display during the GFC.

B. The International Working Group on SWFs and the Santiago Principles

1. Parallel Processes at the IMF and the OECD

Concurrent with their rapid emergence and in direct correlation to the important position SWFs assumed as they moved to plug the balance sheets of a number of major financial institutions (discussed above), cries also began to ring out - from various quarters - by those who were either skeptical or even hostile towards these entities and who hoped to warn the world of some of the perceived dangers of SWFs.[122] Simon Johnson, writing at the time in his capacity as Director of the IMF's Research Department, wrote in September 2007, that "it's time, before the debate becomes politically charged or part of an election campaign, to begin a constructive discussion on the salient issues."[123] Several months later, in March of the following year, it was Jaime Caruana, Director of the IMF's Monetary and Capital Markets Department, who opined that "[a] better understanding of the role and practices of SWFs and the development of a set of best practices could help countries with SWFs benefit from the experience of other countries, strengthen their domestic policy frameworks and institutions, and further their macroeconomic and financial interests".[124] In addition, Caruana also noted that "best practices and principles could also help ease concerns about SWFs in recipient countries and contribute to an open global monetary and financial system". These comments were made at a press conference immediately following a meeting of the IMF's Executive Board, at which it "gave the green light for further analysis on the role of SWFs in the global economy and endorsed a proposal for the IMF to work with SWFs and other relevant parties to prepare a set of best practices for the state investment institutions."[125] Some two months later, at a meeting of countries with SWFs in Washington from April 30–May 1, The International Working Group of Sovereign Wealth Funds (IWG) was established.[126] This process was ultimately to culminate in the elaboration and adoption of the Generally Accepted Principles and Practices, otherwise known as the "Santiago Principles" (discussed below).

It seems reasonable to assume that, at the start of 2008, when the global economic outlook was quickly becoming decidedly cloudy, and with the United States then heading into the final 11 months of a presidential election race, many of the governments behind SWFs felt it might be prudent to act preemptively and establish these principles in order to assuage peoples' worst fears and to silence some of their most hysterical critics. Nevertheless, the governments behind SWFs, not wanting to give a *quid* without a *quo*, also demanded that recipient countries for their part take steps to make investment regimes more predictable. This sentiment was perhaps best expressed by Bader M. Al Sa'ad, Managing Director of the Kuwait Investment Authority, during his keynote speech at the Luxembourg Foreign Trade Conference in April 2008. Al Sa'ad noted that "[if] a set of principles or codes of conduct are established for Sovereign Wealth Funds, then recipient countries should also

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[122] See footnote 114 supra; see also Gilson & Milhaupt (2007-2008) at p. 1346 (footnote 4) who provide the following inventory: Bob Davis, "U.S. Pushes Sovereign Funds to Open to Outside Scrutiny", in: *Wall Street Journal* February 26, 2008; Robert M. Kimmitt, "Public Footprints in Private Markets: Sovereign Wealth Funds and the World Economy", in: *Foreign Affairs* January/February 2008; Peter Thai Larsen, "SWFs Warned to Adopt Code", in: Financial Times, January 23, 2008; James Surowiecki, Sovereign Wealth World, New Yorker, November 26, 2007.

[123] Johnson (2007), at p. 57.

[124] See: "IMF Board Endorses Work Agenda on Sovereign Funds" at http://www.imf.org/external/pubs/ft/survey/so/2008/NEW032108A.htm (November 23, 2011).

[125] *Ibid*.

[126] International Working Group on Sovereign Wealth Funds. (2008), at p. 1.

have the same set of principles for all pools of capital, including Hedge Funds, Private Equity Funds, Pension Funds, Savings Funds, and other non-listed funds, in OECD and non OECD countries."[127]

And so it was that while the governments behind SWFs were drafting the Santiago Principles, another set of governments at the OECD were also formulating a coordinated response to the challenges posed by this new group of investors, a process which culminated, in June 2008, in the OECD Declaration on Sovereign Wealth Funds and Recipient Country Policies.[128] These policies essentially recognize the positive contribution SWFs can make to economic development in the recipient countries, while at the same time acknowledging that SWFs could be a source for concern if their investment strategies were driven by anything other than purely commercial or economic considerations. Finally, the OECD Declaration on SWFs reaffirmed the long-standing principles of a liberal investment regime, non-discrimination in applying any investment barriers and transparency, proportionality and accountability when invoking national security concerns in the context of investment safeguards.

I turn our focus now to the Santiago Principles and to what extent, if at all, they seek to constrain the actions of sovereign governments when they take to the international economic stage as market participants.

2. *The Generally Accepted Principles and Practices: The "Santiago Principles"*

The Santiago Principles, which emerged over a series of three meetings between April and September 2008, the last of which took place in Santiago, Chile, were established in recognition, by those countries with SWFs, of the importance to "demonstrate - to home and recipient countries, and the international financial markets - that the SWF arrangements are properly set up and investments are made on an economic and financial basis".[129] The IWG professes to four over-arching principles guiding the 24 rules which constitute the GAPP[130], namely[131] 1) a desire to help in maintaining "a stable global financial system and free flow of capital and investment; 2) compliance with "all applicable regulatory and disclosure requirements" in the host countries; 3) investments motivated by "economic and financial risk and return-related considerations"; and 4) having in place a "transparent and sound governance structure that provides for adequate operational controls, risk management, and accountability".

In preparing the Santiago Principles, the IWG commissioned a report, written by three IMF economists[132], to survey prevailing institutional arrangements and operational practices.[133] Some elements of the GAPP seem to have been taken from this survey, while others are the product of what the IWG refers to as "a distillation of principles and practices applicable to SWF activities that are already in use in other international *fora*".[134] By way of reference in this context, the IWG lists a

127 Quoted in Mostrous, Gue & Dittman (2011), at p. 36.

128 Available at: http://www.oecd.org/officialdocuments/displaydocumentpdf?cote=C/MIN%282008%298/FINAL&doclanguage=en (November 23, 2011).

129 International Working Group on Sovereign Wealth Funds. (2008), at p. 4.

130 Note that the terms "GAPP" and "Santiago Principles" are used synonymously, and may sometimes be referred to here as the "Principles" or the "24 Principles".

131 *Ibid*.

132 Note that one of the authors, Cornelia Hammer, was on secondment at the IMF from the *Deutsche Bundesbank*. The other two individuals were Peter Kunzel and Iva Petrova, both working in the Monetary and Capital Markets Department of the IMF.

133 See: Hammer, C., Kunzel P, & Petrova I (2008); in addition to being released as an IMF Working Paper, this report was also published under the auspices of the IWG Secretariat in Collaboration with the Members of the IWG.

134 International Working Group on Sovereign Wealth Funds. (2008), at p. 4.

number of such sources, including several best practices guidelines for the hedge fund and insurance industries, as well as codes of conduct for accountants and foreign exchange reserve managers.[135]

The stated purpose of the Santiago Principles is to "identify a framework of generally accepted principles and practices that properly reflect appropriate governance and accountability arrangements as well as the conduct of investment practices by SWFs on a prudent and sound basis."[136] Adherence to the GAPP is completely voluntary, and no formal enforcement mechanism is provided. Indeed, the GAPP seems to constitute as much an aspirational document as it does a code of prevailing practices, since the IWG itself states that its members have either implemented these principles and practices or "aspire" to do so.[137]

The IWG divides its 24 Principles into three main subsets, or what it refers to as "key areas". These are "(i) legal framework, objectives, and coordination with macroeconomic policies; (ii) institutional framework and governance structure; and (iii) investment and risk management framework."[138] For the purpose of the analysis to be conducted here, the following principles are arguably the most relevant:

- **GAPP Principle 2** The policy purpose of the SWF should be clearly defined and publicly disclosed;
- **GAPP Principle 4** There should be clear and publicly disclosed policies, rules, procedures, or arrangements in relation to the SWF's general approach to funding, withdrawal, and spending operations;
- **GAPP Principle 6** The governance framework for the SWF should be sound and establish a clear and effective division of roles and responsibilities in order to facilitate accountability and operational independence in the management of the SWF to pursue its objectives;
- **GAPP Principle 9** The operational management of the SWF should implement the SWF's strategies in an independent manner and in accordance with clearly defined responsibilities;
- **GAPP Principle 14** Dealing with third parties for the purpose of the SWF's operational management should be based on economic and financial grounds, and follow clear rules and procedures;
- **GAPP Principle 16** The governance framework and objectives, as well as the manner in which the SWF's management is operationally independent from the owner, should be publicly disclosed;
- **GAPP Principle 17** Relevant financial information regarding the SWF should be publicly disclosed to demonstrate its economic and financial orientation, so as to contribute to stability in international financial markets and enhance trust in recipient countries;
- **GAPP Principle 18** The SWF's investment policy should be clear and consistent with its defined objectives, risk tolerance, and investment strategy, as set by the owner or the governing body(ies), and be based on sound portfolio management principles;
- **GAPP Principle 19** The SWF's investment decisions should aim to maximize risk-adjusted financial returns in a manner consistent with its investment policy, and based on economic and financial grounds;
- **GAPP Principle 20** The SWF should not seek or take advantage of privileged information or inappropriate influence by the broader government in competing with private entities;

[135] *Ibid*, at p. 49.
[136] *Ibid*, at p. 4.
[137] *Ibid*, at p. 5
[138] *Ibid*.

- **GAPP Principle 21** SWFs view shareholder ownership rights as a fundamental element of their equity investments' value. If an SWF chooses to exercise its ownership rights, it should do so in a manner that is consistent with its investment policy and protects the financial value of its investments. The SWF should publicly disclose its general approach to voting securities of listed entities, including the key factors guiding its exercise of ownership rights.

It becomes clear from a cursory read of these excerpts from the GAPP that the document seeks to address some of the most obvious criticisms leveled at SWFs and to assuage the concerns of those who see them as the instrument of choice for some kind of government-funded global financial conspiracy to shift the balance of power from the developed world to a handful of newly emerging economies.

C. Criticism of SWFs and the Santiago Principles

The reasons why SWFs have come in for criticism have already been discussed above in some detail, but essentially boil down to an inherent distrust by many governments of other governments trying to usurp market forces. Whereas the motives for private hedge funds or other sizeable investors such as pension funds are evident (to maximize return on investment at various levels of risk exposure), the motives of any entity owned by a sovereign are, rightly or wrongly, intrinsically more suspect. To counter such suspicions, much of what the Santiago Principles aim to achieve is assuring policymakers and other observers of their commitment to market forces, their operational independence and of the transparency with which they conduct themselves.

Some commentators dismiss the Santiago Principles as "artefacts of soft law" given the fact that they constitute little more than "non-binding principles, private 'naming and shaming' indices, informal alliances, and ‘'soft institutions'—voluntary fora that lack legal personality."[139] Wong essentially lists four grievances he has with the Santiago Principles. Having first identified a number of reasonable objections many have towards SWFs, the most important of which is asymmetrical information between host country and the SWF, Wong lists four shortcomings of the Santiago Principles, namely:[140] (1) the Principles are "too focused on SWFs as entities and not enough on their relationship with recipient countries"; (2) the lack of benchmarks to "measure compliance with or achievement of the Principles"; (3) that the Principles fail to address the underlying problem of asymmetrical information; and finally (4) the lack of any credible sanctions system "to ensure compliance".

Although much of the criticism rightly focuses on the purely voluntary nature of these principles and the lack of hard sanctions for their breach, this overlooks the fact that much if not all of governments' undertakings in the area of international financial or monetary cooperation tends to be of a predominantly soft law nature.[141] Moreover, despite the authors of the GAPP seeking inspiration in the rules governing the hedge fund, insurance and accounting industries, these are still early days yet for international cooperation on SWFs, so governments can hardly be blamed for not wanting to tie their hands too tightly and too soon. Only time will tell whether the Santiago Principles have gone far enough in soothing the fears of policymakers and investors. The dynamism of global capital markets will also be an arbiter of whether SWFs represent the most efficient means for governments to manage their surplus foreign exchange.

[139] Gelpern (2011), p. 290.
[140] Wong (2009) p. 168
[141] See Brummer (2012).

IV. NASCENT AND EMERGING MULTILATERAL RULES TO DISCIPLINE STATE OWNED ENTERPRISES

Various definitions seem to abound for what constitutes an SOE[142]. For the purposes of this paper, given that STE's and SWFs have each been discussed separately, the working definition used here shall be that of a commercial entity in which a local, regional or federal government has direct or indirect control by virtue of its ownership of either the entity's equity or its operating assets. These entities distinguish themselves from both STEs and SWFs by the fact that the majority of their revenues come from selling goods and services.[143]

State-Owned Enterprises tend to defy neat categorization in terms of the typologies for government intervention provided at the beginning of this paper. More often than not they are a vehicle for economic development (particularly in the context of a government-led drive to achieve industrialization), or they may be an expression of a country's strategic trade policy. Chang (2007) defends the utility of SOEs by describing their perceived unique abilities to provide public goods which market actors might be insufficiently willing to provide[144], which essentially constitutes a variation of the market failure rationale for state intervention.

State-Owned Enterprises play a very important role in many economies and across various economic sectors, but they have become a particular focus of attention for international observers and western policymakers in China and Russia, where, for structural reasons involving these countries' transition from planned to market economies, they are still particularly prevalent. Whereas in the 1990s the emphasis in many countries was privatization of SOEs, the focus seems to have shifted more recently to both the competitive efficiency of SOEs[145] as well as the need to have them adhere to generally recognized principles of sound corporate governance. In the trade arena, rules are slowly taking shape to mitigate some of the more damaging practices of SOEs. We discuss first the principles emerging from the OECD before looking at what has been going on at the WTO.

A. Ongoing Efforts in the OECD

Work in the OECD on this issue has largely been taking place in the context of the Organization's Working Party on State Ownership and Privatisation Practices, and has been conducted under the auspices of the Corporate Affairs Division of the Directorate for Financial and Enterprise Affairs.[146] In fact, a significant body of applied research and policy advice has been produced on the privatization processes of major transition economies such as Russia and China, with a view to improving corporate governance in the State-owned sector and in transition economies in general. One report notes that, despite the progress that has been made over the last two decades, "problems remain, not least in the network industries where many remaining SOEs are market incumbents that continue to enjoy monopolies in part of their value chains or government subsidies, purportedly in compensation for public service obligations."[147] The OECD's main policy response to the problems of poor corporate governance in the State-owned sector and the inherent economic inefficiencies and welfare losses this creates, has been the development of so-called "competitive neutrality frameworks" which a

[142] See, for example OECD (2009) at p. 5.

[143] This definition incorporates elements borrowed from Privatization Barometer, a non-government organization originally set up to monitor and report on the privatization process going on in EU enlargement countries; see: http://www.privatizationbarometer.net/; see also http://www.privatizationbarometer.net/site/definitions.pdf (November 23, 2011).

[144] Chang (2007) at p. 6.

[145] See The Economist (2012)

[146] See http://www.oecd.org/department/0,3355,en_2649_34795_1_1_1_1_1,00.html (January 27, 2012).

[147] The same could be said of many network industries in developed market economies; see Capobianco and Christiansen (2011), p. 3.

number of OECD member countries have implemented. These have been accompanied by OECD Guidelines on such issues as privatization and corporate governance of SOEs.

The OECD cites a definition of competitive neutrality used by the Australian Productivity Commission. It states that "competitive neutrality requires that government business activities should not enjoy net competitive advantages over their private sector competitors simply by virtue of public sector ownership."[148] Some of the advantages cited include:[149] (1) outright subsidization; (2) concessionary financing and loan guarantees; (3) other preferential treatment by government; (4) monopolies and advantages of incumbency; (5) captive equity; (6) exemption from bankruptcy rules; and (7) information advantages. A number of reasons are given for the continued existence of SOEs including maintaining public service obligations, serving as a tool for industrial policy, the protection of a public revenue stream, and political-economy imperatives.

Competitive neutrality frameworks are therefore generally directed at dealing with the underlying rationales for maintaining SOEs while simultaneously trying to remove any concessionary or preferential treatment these firms may enjoy vis-à-vis other market participants, with the onus being on incrementally exposing the SOE to an increasing degree of market discipline. Competitive neutrality frameworks are also an effective strategy for preparing a given sector for increased competition as a result of future trade liberalization that has either been committed to by the government or which it intends to commit to in the context of impending trade negotiations. As we will see below, the gradual phasing out of SOEs or the removal of their privileged status has been a consistent focus of WTO accession negotiations.

B. The WTO and Commitments by Recently Acceded Members

Except in a few limited cases involving newly independent states in the 1990s, who had embarked on an ambitious program of economic reform and who were willing to make almost any concession to enter the WTO, accession to the global trading body has generally tended to be a long, drawn-out, and difficult process. In addition to the relatively extensive market opening commitments applicants are required to offer, they are also expected to make far-reaching changes to their internal economic systems, particularly if they are transition economies. Part of this process involves commitments to reform or abolish any SOEs that might be playing a major role in sectors where WTO Members have export interests of their own.

A look at the Chinese Working Party Report adopted as part of its WTO accession package shows that the Government of China was required to provide the usual commitments in the form of the following undertaking:[150]

> "China would ensure that all state-owned and state-invested enterprises would make purchases and sales based solely on commercial considerations, e.g., price, quality, marketability and availability, and that the enterprises of other WTO Members would have an adequate opportunity to compete for sales to and purchases from these enterprises on non-discriminatory terms and conditions. In addition, the Government of China would not influence, directly or indirectly, commercial decisions on the part of state-owned or state-invested enterprises, including on the quantity, value or country of origin of any goods purchased or sold, except in a manner consistent with the WTO Agreement"

[148] *Ibid*, p. 5.
[149] *Ibid*.
[150] See Report of the Working Party on the Accession of China (WT/ACC/CHN/49) dated 1 October 2001, para. 46 (p. 9)

The more recent and still pending accession of Russia also shows that this was a concern for WTO Members for what was perceived as the wide-spread and deeply intrusive involvement of the state in government owned or government-controlled enterprises. The Russian representative was required, at various sections in the Working Party report to make repeated representations to assuage the fears of WTO Members, who explained their expectations as follows:

> "Members of the Working Party stated that they expected the Russian Federation to ensure that the practices of State-owned, State-controlled enterprises and enterprises enjoying special or exclusive privileges would be brought into line with relevant WTO requirements as from the date of accession. These Members asked for confirmation that, upon accession, purchases and sales by such enterprises, whether State-owned, State-invested or enjoying any special or exclusive privileges, would be based solely on commercial considerations, without any Government influence or application of discriminatory measures" [151]

The Russian representative ultimately had no choice but to offer undertakings that these expectations would be met.

V. Findings and Conclusions

We have seen that it has proven very difficult to constrain the actions of sovereigns once they enter markets in the guise of a corporate entity, regardless of whether this is in the form of a state trading enterprise, sovereign wealth fund or state-owned enterprise. This is likely due to a number of reasons, including the fact that sovereigns are not particularly enamored of hard constraints on their actions and because they often avail themselves of these entities to pursue policy objectives they consider more important than international cooperation.

Nevertheless various approaches may prove successful at curbing the more egregious and market-distorting practices of some of these entities, such as binding export subsidy disciplines for exporting STEs, or the promotion of competitive neutrality frameworks underpinned by the hard logic of economic efficiency arguments for SOEs. Efforts to achieve greater transparency for SWFs and the desire of their owners to be welcomed in foreign capital markets will inevitably constrain these vehicles from engaging in practices that are perceived as potentially suspect or dangerous for the stability of the financial system as a whole.

International cooperation on these issues is likely to continue on the course so far embarked upon, namely eschewing hard and binding rules for the policy space that comes with softer, non-binding and non-enforceable principles and aspirational documents.

[151] See Report of the Working Party on the Accession of Russia (WT/ACC/RUS/70) dated 17 November 2011, para. 98 (p. 25)

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