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INTERIM REVIEW OF PROGRESS IN THE IMPLEMENTATION OF THE WORK PROGRAMME ON ELECTRONIC COMMERCE

Communication from the Chairman of the Council for Trade in Goods

The following communication, dated 9 April 1999, addressed to the Chairman of the General Council by the Chairman of the Council for Trade in Goods is circulated to Members.

At the Council for Trade in Goods' informal meeting on electronic commerce of 8 March 1999, Members requested the Chairman to prepare a factual summary on the status of discussions after the conclusion of a series of informal meetings of the Council for Trade in Goods (held on 26 November 1998, 5 February and 8 March 1999) on aspects of electronic commerce relevant to the goods area. The Chairman was asked to convey this summary to the Chairman of the General Council as input for the interim review of progress in the implementation of the work programme which the General Council is set to conduct on 14 April 1999.

I herewith enclose the text of this summary which reflects the status of discussions on the items listed in paragraph 3.1 of the work programme after the informal meetings chaired by my predecessor, Ambassador Saborio Soto.

Members agreed to continue their discussions on electronic commerce, if required, in light of the results of the interim review of progress in the implementation of the work programme.

COUNCIL FOR TRADE IN GOODS WORK PROGRAMME ON ELECTRONIC COMMERCE

Chairman's summary of the discussions held in the CTG

Members requested the Chairman of the Goods Council to prepare a factual summary on the status of discussions after the conclusion of a first round of informal meetings of the Council for Trade in Goods on aspects of electronic commerce relevant to the goods area. The Chairman was asked to convey this summary to the Chairman of the General Council as input for the interim review of progress in the implementation of the work programme which the General Council is set to conduct on 14 April 1999.

1. Introduction

1.1 Paragraph 3.1 of the Work Programme on Electronic Commerce (WT/L/274, 30 September 1998) mandates that "the Council for Trade in Goods shall examine and report on aspects of electronic commerce relevant to the provisions of GATT 1994, the multilateral trade agreements covered under Annex 1A of the WTO Agreement, and the approved work programme. The issues to be examined shall include:

- market access for and access to products related to electronic commerce;
- valuation issues arising from the application of the Agreement on Implementation of Article VII of the GATT 1994;
- issues arising from the application of the Agreement on Import Licensing Procedures;
- customs duties and other duties and charges as defined under Article II of GATT 1994;
- standards in relation to electronic commerce;
- rules of origin issues;
- classification issues."

1.2 In order to discharge its mandate, the Goods Council held three informal meetings (on 26 November 1998, 5 February and 8 March 1999) where it discussed the issues listed above. The Secretariat produced a note (G/C/W/128) that provides background information on these issues. The following factual summary of the discussions in the CTG seeks to reflect the views expressed at the three meetings.

1.3 A central element of the discussions at all three meetings was the question of characterization of electronic transmissions as services, goods or something else, as well as practical problems related to this question. The issue was brought up under several headings (i.e., customs duties, classification, customs valuation, rules of origin, and import licensing). For reasons of cohesiveness of the arguments made, it appears useful to synthesize the debate under a separate heading "characterization."

2. Scope of the work programme and characterization of electronic transmissions

2.1 Some delegations were concerned that the term electronic commerce had not been defined and believed that work should start by developing such a definition. Other delegations noted that a definition was only useful insofar as it had relevance for the existing commitments, and feared that any effort to devise a definition would be difficult in an evolving and dynamic area such as electronic commerce. One delegation stated that a definition of electronic commerce itself was not necessary in the context of the work programme, as the Goods Council could tackle the issues listed in paragraph 3.1 without further definition. As no WTO commitments existed on electronic commerce *per se*, no end-definition of the term was needed.

2.2 In the context of the discussion of what elements electronic commerce comprises, one delegation suggested considering four categories of transactions that would fall under the working definition of e-commerce:

- (i) electronically conducted transactions combined with physical delivery of goods; in this case the traditional GATT commitments would apply;
- (ii) trade in goods related to electronic commerce (e.g. computers); also in this case, the traditional GATT commitments would apply;
- (iii) sale of carrier media such as CD's or tapes, which contain digitalized information (e.g., software or music); the question of content of the carrier media would relate to customs valuation questions;
- (iv) digitalized information transmitted by electronic means, i.e. electronic transmissions.

2.3 There was a prevalent perception by most delegations that it was necessary to characterize electronic transmissions. The WTO provisions in the goods area (i.e., the GATT 1994 and the multilateral trade agreements covered under Annex 1A of the WTO Agreement) would be relevant for electronic transmissions where and in as far as the content of these transmissions could be qualified as goods.

2.4 Some delegations stated that the electronic transmission of data itself was a delivery service, which was covered by the General Agreement on Trade in Services (GATS). One delegation wondered whether the contents of electronic transmissions could be separated from the supply of the contents, while another delegation saw merit in separating content and supply.

2.5 Some delegations stated that electronic transmissions were always to be considered services, and the disciplines developed under the GATS would apply. The GATS was technology neutral and would not discriminate between different modes of delivery. Other delegations responded that this failed to take into account the dynamic and evolving nature of the Internet.

2.6 Some delegations raised the question whether the legal disciplines of the GATT could be applied to digitalized contents delivered through electronic means, in as far as these contents could be characterized as goods. The contents of some electronic transmissions did resemble or were close substitute to goods. Examples given in this context related to music downloaded from the internet in the form of digitalized data vs. a physical CD purchased in a shop. In the circumstances where software downloaded from the Internet was a perfect substitute for software on a disk or CD, questions would arise why customs duties should be levied only on the physical product (if imported from abroad) yet not on the downloaded data. However, it was noted that downloaded data might not fall under the definition of an import. It was further noted that, in the future, software downloaded over the internet would likely result from a series of interactions between customer and vendor and

the download would not be a “like” product. Thus, it was thought that it may be useful to have a discussion regarding “like products” in this context.

2.7 One delegation considered that mass distribution of data through electronic transmissions should fall under the GATT disciplines, while more personalized distributions should be covered by the GATS.

2.8 One delegation believed that it would not be productive to force whatever might transpire through electronic transmissions into familiar categories such as goods or services. All digitalized products could be traded over the internet, and while some products, e.g. software or music, could be stored on carrier media after having been received electronically (thus approximating a good), a carrier media was in many cases unnecessary. Products could also be stored on the computer’s hard drive of the recipient. Exhibiting permanence, but no fixed tangible form, such products would raise questions as to whether they fit into the category of goods or services. The inherently ‘customizable’ nature of many digital products would argue against classifying them as traditional goods. The number of new categories of products made possible by digitalization was limitless. For example, digitalized products often combined elements that in physical applications were separate, such as by combining educational, entertainment and even business applications in a single product.

2.9 Another closely related aspect addressed the question of whether an importation did take place when transmitting data electronically. One delegation stated that, where customs duties were applied to goods in the delegation’s country, a cross-border trade transaction was always involved. With electronic commerce, especially in the internet realm, it was unclear whether there was a ‘thing’ that actually moved across a border, which would lead to the conclusion that an “importation” in the sense of Article II of the GATT had not taken place. GATT Article II referred to customs duties applied in connection with an importation. If no importation was involved, electronic transmissions would be taken out of the realm of applying customs duties.

2.10 Another delegation believed that it was difficult to see how a distinction between “goods” and “services” could be handled in practice, even if agreed on in theory. As the transmitted bytes of data streams consisted only of one’s and zeroes, the delegation raised the questions how it was possible to decide for each individual case whether a particular transmission was covered by goods or services disciplines?

2.11 The discussions showed that there was a wide range of opinions and questions regarding the characterization of the content of electronically transmitted digitalized data, including the question whether such a characterization was actually bringing discussions on the work programme forward.

3. Market access for and access to products related to electronic commerce

3.1 Several delegations stated that the market access commitments for products related to electronic commerce were laid out in the existing schedules of Members. It was mentioned by many Members that the conduct of trade by electronic means would not change the obligations laid down in the tariff bindings contained in Members’ schedules. Two delegations stated that the question of access to products in question was under the purview of each and every country itself.

3.2 Diverging views were expressed about the relevance of the Information Technology Agreement (ITA) for this subject. Several delegations believed that the ITA was an important contribution to providing a conducive environment for electronic commerce by providing less expensive access to electronic commerce related products, thus boosting participation in electronic commerce among its participants. Some delegations believed that the list of products covered by the ITA was roughly coextensive with electronic commerce related products, so that no separate

programme of work to improve market access for these goods was needed. Participation in the ITA by a larger number of Members would enhance market access for these products. Other Members believed that the relevance of the ITA for the question of market access for and to electronic commerce related products was limited, as not all WTO Members were participants in this Agreement. Therefore, a wider perspective of analysis should be taken. Also, the list of relevant products might extend beyond the products covered by the ITA. A few delegations believed that the ITA did not bear any relevance for the current work programme, as the ITA was a sectoral agreement with no relationship to questions related to electronic transmissions.

3.3 As concerns the link between electronic commerce and trade facilitation, some delegations maintained that this topic was of no relevance to the work programme, because the use of electronic means to facilitate the flow of goods was not connected to the 'production, distribution, marketing, sale or delivery of goods and services by electronic means,' which was the definition of electronic commerce in paragraph 1.4 of the work programme. Other delegations believed there was a close linkage between both issues. One delegation noted that one trade facilitation issue with relevance to electronic commerce were policies or practices regarding electronic transactions in Member countries which may either help or hinder the development of electronic commerce products.

3.4 *The following additional comments were made:*

- One delegation suggested to discuss in greater detail linkages between the ITA and products that are necessary elements in the conduct of electronic commerce.
- Another delegation wondered if, and to what extent, market access to the products in question was restricted through export restrictions, e.g. for security reasons.
- It was asked whether tariffs on electronic commerce related products would impede the ability of countries to develop the necessary infrastructure for electronic commerce?
- One delegation believed that, while some discussion had been held about market access for electronic commerce related products, more needed to be known about access to those products in the importing countries.

4. Customs duties and other duties and charges as defined under Article II of GATT 1994

4.1 Delegations stressed that the Ministerial Declaration on Electronic Commerce (WT/Min(98)/DEC/2) provided for a standstill regarding customs duties on electronic transmissions, while the work programme on e-commerce mandated examination of a wider range of issues, e.g. questions related to the sale of physical goods by electronic means. It was stated that the standstill agreement could in no way prejudice the outcome of the work programme.

4.2 There seemed to be agreement by delegations that goods that were sold or marketed by electronic means, but still delivered physically across borders, would be subject to the existing WTO commitments and provisions related to trade in goods, e.g. customs duties.

4.3 Several delegations were of the opinion that the application of customs duties and other duties and charges as defined under Article II of GATT 1994 would only be possible insofar as electronic transmissions were considered goods. One delegation added that another prerequisite was that the transmission was clearly defined as an importation. This delegation believed that both these premises were questionable. A more detailed discussion of this question is contained in the section on characterization, above.

4.4 One delegation raised the question that, even if it was possible to single out certain transmissions as goods (with the consequence that customs duties could be applied), how could the applicable customs rate be determined, in particular, as electronic transmissions were currently not classified in the Harmonized System (HS) or in tariff schedules of Members? Also, would classification for customs purposes not depend on the content of the transmitted goods?

5. Classification issues

5.1 Several delegations stated that the HS would not seem suitable to classify electronic transmissions, as these were services, while the HS was a nomenclature for the classification of goods. "Content" itself was not dealt with in the goods agreements, but appeared to be an intellectual property question. Therefore, the TRIPS Council should address this issue. Other delegations believed that classification was a cross-cutting issue with services and TRIPS.

5.2 One delegation argued that the classification of goods generally relied on the distinguishing physical characteristics of the product. This was also true for the classification of analogue carrier media "information" products (e.g., maps, books, LP records, video cassette tapes, etc.) However, digitalization had made classification more problematic, as digital products on physical carrier media were approaching a state where it was increasingly difficult to characterize the type of product based on physical appearance or physical characteristics. Discs for laser reading systems, for example, had increasingly the capability to operate across a wide range of 'platforms,' from traditional computer devices to laser disc readers used for other applications. Ultimately, such CD's merely consisted of representations of zeroes and ones.

5.3 Another delegation stated that the HS was devised for the purpose of collecting customs duties and trade statistics. On electronic commerce there was already a standstill commitment to continue the current practice of not imposing customs duties. The collection of statistics would in any case be difficult due to the nature of electronic transmissions.

5.4 Members were informed that a WCO member country had, within that forum, recently made a proposal to separately identify "software without carrying media" in the HS. Furthermore, the HS had a provision for the classification of electrical energy (heading 27.16), which was an intangible commodity. However, this heading was optional, and its use was left to the discretion of HS Contracting Parties.

6. Valuation issues arising from the application of the Agreement on Implementation of Article VII of the GATT 1994

6.1 One focus of the discussion on customs valuation issues relevant to the work programme concerned the "Decision on the Valuation of Carrier Media Bearing Software for Data Processing Equipment" (VAL/8), which gives Members the option to levy customs duties either on the basis of the transaction value (the price paid or payable) for the carrier media (e.g. diskette) including the value of the software, or alternatively on the basis of the cost or value of only the carrier medium itself.

6.2 Several delegations stated that the relevance of the Decision was limited for the discussions under the work programme, as its scope did not extend to electronically transmitted data, or sound and image recordings. It was noted that the Decision did explicitly exclude sound, cinematic or video recordings, the transmission of which through electronic means had become increasingly popular.

6.3 Some delegations believed that where a carrier medium did not exist, services rather than goods were concerned, and discussions on services related aspects would come up in the Council for Trade in Services. For the case that a carrier medium existed, the non-physical information contained thereon had been treated as a good, because no Agreement on Services existed in 1984, when the Decision was taken.

6.4 Other delegations believed that it should at this stage not be excluded that electronic transmissions could be considered goods, for which case the Customs Valuation Agreement was relevant, and valuation issues based on that Agreement could arise.

6.5 One delegation saw some significance in the fact that the Decision represented a conclusion that the imported product was more accurately described as simply the carrier medium, even though in terms of interest to the importer the carrier medium was incidental. Thus, the data itself was not an importation. This was also reflected in the 1984 Decision, where the Chair of the Committee on Customs Valuation stated that 'software can be transmitted by wire or satellite, in which case the question of customs duties does not arise' (VAL/W/14/Rev.2, 25 July 1984).

6.6 One delegation believed that in the commercial electronic transmission of software, the buyer was actually purchasing a licence and not the programme *per se*. The programme remained the property of the company that produced it and distributed it. In this context, the valuation of services in electronic commerce needed to be addressed, whereby it was relevant to consider not so much the value of the software *per se* or the particular information it consisted of, but rather the value of the licence or the right to use what was being transmitted.

6.7 One delegation stated that electronic payments for the imported good (such as credit card payments over the internet) could pose problems with regard to the valuation of goods, if domestic banks were not involved in the transaction. Improper valuation of imported products paid for electronically would constitute a major problem.

7. Rules of origin issues

7.1 It was stated that rules of origin themselves were a tool for applying other trade policy instruments, such as tariffs or bilateral quantitative restrictions, and it was hence difficult to evaluate their relation to electronic commerce before determining how other instruments that require a rules of origin determination for their application should apply in the context of electronic transmissions. Several delegations considered it premature at this stage to discuss rules of origin issues, but argued that the Agreement on Rules of Origin may apply if electronic transmissions were determined to be goods.

7.2 One delegation stated that rules of origin for data had been discussed in the context of the harmonization work programme on rules of origin. During the debate on rules of origin for recorded media or sound recordings (HS Code 8524) there had been a proposal to confer origin to the country where recordings were produced by photographic producers located or established in that country (as opposed to where the sound is copied onto a carrier medium). However, these discussions had remained inconclusive. The same delegation stated that in case an origin determination was based on *ad valorem* criteria, the question of the value of the data contained in a final product was not unique to the case where that data was electronically transmitted. The same problem would arise if the data was transmitted through non-electronic means.

7.3 One delegation pointed out that the use or embedding of information was becoming very commonplace for virtually every manufactured product from smart microwave ovens to internet-connected automobiles and toys. In this sense all manufactured products were becoming carrier

media for digitalized information, however these situations would generally present traditional issues pertaining to treatment of a physical good, and not of electronic transmission of digitalized data. Historically, in the context of preferential origin regimes that applied value-added content thresholds, the inclusion or the exclusion of costs for particular intangible items used in the production of goods was not unusual. However such practices did not involve a search for the origin of data. They rather pertained to ascertaining costs related to the production of the physical good in question for which the origin needed to be determined. On the question of electronic transmissions, the fluid nature of the environment for electronic commerce, i.e. the flow of constantly evolving pieces, of functionality, processing and communication was mentioned.

7.4 Another delegation stated that the case pointed out in section 6.3 of document G/C/W/128, i.e. the case where data was sent electronically and stored in a physical carrier medium was important, although origin questions might arise even if the data was not transmitted electronically. The delegation also believed that the Committee on Rules of Origin and the WCO Technical Committee were suitable fora to discuss this kind of question.

7.5 Several delegations stated that the determination of the origin of electronic transmissions (for those which might be classified as goods) would create difficulties. Sophisticated technology, allowing for easy duplication and unlimited routing of digitalized data made it difficult to find out where a transmission actually originated. One delegation noted that transmissions themselves were not single point-to-point transactions. Where borders were crossed by such transmissions was contingent at any time on the specific particularities of the networked array of users combined with similarly changing particularities involving routine and placing of machines such as servers. Such an environment was not a medium of convenience that competed with or was even parallel to definable, individual, cross-border transactions. Hence there existed very serious doubts as to the applicability of rules of origin to an electronic commerce setting.

8. Standards in relation to electronic commerce

8.1 One delegation raised the issue of promoting international standardization relevant to electronic commerce, and emphasized that measures and procedures for establishment and application of standards should not themselves become trade barriers or an impediment to the competitive development, transfer and dissemination of technologies related to the global information infrastructure. The global information infrastructure, which covered both information systems and telecommunications, formed the basic platform through which global electronic commerce was conducted and allowed interconnectivity and interoperability of domestic information communications infrastructures. Accordingly, standards played a more dominant role in global electronic commerce than in other commodity transactions, as global electronic commerce required standardization of both commodity and the medium. Mismatches of standards not only restricted trade but also infused non-synchronisation of operations, thus indirectly breeding monopolies and cartels in the global market. The delegation further noted that the TBT Agreement which had been established to remove the inherent discrepancies arising from uneven standardization so that the free flow of trade was facilitated did provide disciplines regarding adherence to international standards specified by ISO and the IEC through consensus. The delegation underlined the importance of involving developing countries and small and medium sized enterprises in the development and establishment of technological standards for software applications and electronically traded commodities to ensure interoperability, connectivity, and access to platforms for electronic commerce for them. It identified several issues that would merit further discussion: (i) development and application of standards for software applications; (ii) disadvantages for domestic information infrastructure, particular of developing countries, due to rapid technological changes influenced by dominant market players, monopolies and cartels; (iii) encryption technology; (iv) cartelization of the telecommunications equipment market; (v) compatibility of protocols and hardware equipment to

ensure interoperability and interconnectivity of systems; (vi) standards for content (commodities traded in digitalized form); (vii) market dominance of few companies as an impediment to interoperation and interconnection.

8.2 Other delegations, in preliminary reactions to the above statement, believed that excessive government regulation and reliance on mandatory standards would inhibit technological development, thus slowing their potential benefits. Ultimately a balance needed to be struck between the benefits of dynamic private research and development, while safeguarding these developments against monopolies of technology that themselves would introduce serious market distortions and run counter to the legitimate interest of people to benefit from information technology. The current expansion of electronic commerce was based on the freedom of transactions, and standards needed to be developed to promote electronic commerce and not to prevent such a development. It was doubtful that the WTO or any other body would be able to standardize all areas of software and hardware interconnectivity. It was stated that the WTO should aim at developing general disciplines and principles rather than setting specific standards for electronic commerce. A number of delegations stated that the issues raised in paragraph 8.1 could be examined in more detail on the basis of a paper by the delegation which had raised them.

8.3 Several delegations stated, that also the standards question needed to be looked at in the context of characterization of electronic transmission as goods, services or something else. Only for those elements of electronic commerce for which the goods disciplines applied was the TBT Agreement relevant.

9. Issues arising from the application of the Agreement on Import Licensing Procedures

9.1 Delegations who spoke agreed that possible issues could meaningfully be discussed only after further clarification of the character of electronically transmitted data. The issue was similar to the area of rules of origin, or customs valuation.

10. Other issues

10.1 One delegation stated that it was important to see how development concerns related to electronic commerce, and to see how electronic commerce would displace traditional means of trading. Another delegation believed that electronic commerce, rather than displace traditional means of trading, would have a large potential in creating trade and production. Therefore, growth of electronic commerce was not trade restrictive and should not give rise to any restrictions out of fears of displacement.

10.2 Another delegation stated that it would be useful to explore whether a facilitatory framework of general principles could be developed for key aspects of electronic commerce. However, one should move with great caution in areas like consumer protection, security of transactions, and fraud. The delegation had doubts about the enforceability of measures to restrict the electronic provision of certain services in a Member's territory.

11. Concluding note by the Chairman

11.1 On the basis of discussions to date, it appears that a majority of delegations believe that most aspects of electronic commerce delegated to the CTG for discussion can only be meaningfully addressed once a determination has been made if, and under what circumstances, electronic transmissions can be considered as services, goods, or something else. This question of

characterization of electronic transmissions, however, is one of the “trade-related issues of cross-cutting nature”, which, according to paragraph 1.2 of the work programme, the General Council shall take up for consideration. In light of these considerations, Members agreed to continue discussions on this matter, if required, in the context of the results of the interim review of progress in the implementation of the work programme, foreseen in the General Council.
