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TRADE POLICY REVIEW

Reports by

SWITZERLAND AND LIECHTENSTEIN

Pursuant to the Agreement Establishing the Trade Policy Review Mechanism (Annex 3 of the Marrakesh Agreement Establishing the World Trade Organization), the policy statements by Switzerland and Liechtenstein are attached.

[1] Original version in French for the Report by Switzerland and original version in English for the Report by Liechtenstein.

Note: These reports are subject to restricted circulation and press embargo until the end of the meeting of the Trade Policy Review Body on Switzerland and Liechtenstein.

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REPORT BY SWITZERLAND

I. GENERAL COMMENTS

1. This report, together with that of Liechtenstein and the Secretariat report on the two countries, establishes the basis for the review of their trade policy by WTO Members on 15 and 17 December 2004, given the fact that they form an economic and monetary union and Liechtenstein is an integral part of Swiss customs territory.

2. International trade plays a key role in the Swiss economy, accounting for a very substantial proportion of GDP[2], despite the virtual stagnation of foreign trade between 2000 and last year. The Swiss Government attaches great importance to the openness of world markets for goods and services, including government procurement, and to strong protection of intellectual property.

3. Switzerland's economic policy aims at strengthening its *international competitiveness* and is pursued by a *macroeconomic policy* geared to fiscal consolidation, price stability and a return to more buoyant growth, together with the establishment of domestic framework conditions favourable to investment.

4. The Swiss Government has endeavoured to improve the economic environment in recent years by implementing *structural reforms*, despite relatively unfavourable economic conditions. The measures introduced in *domestic policy areas* included a major revision of the Law on Cartels, further liberalization in the telecommunications, railways and postal sectors, an extension of the scope of government procurement, continued reforms in agriculture, and an adaptation of many technical standards to those of the European Union (EU). Moreover, a new seventeen-point structural reform package was introduced in early 2004 to stimulate growth by revitalizing the domestic economy.

5. Switzerland's main priorities in *foreign policy areas* remain economic openness and further liberalization of international trade, at the multilateral, regional and bilateral levels.

6. At the *multilateral* level, the Swiss Government notes that the trend towards faster globalization implies both opportunities and challenges for all parties engaged in international trade. Increased interdependence requires further reinforcement of multilateral cooperation and the relevant institutions. In this connection, the Swiss Government believes that a key role must be assigned to the WTO for the progressive liberalization of international trade, setting up the rules, rights and obligations governing international trade, and dispute settlement. It is also important in this regard to promote consistency in external economic policy activities and other government policies on both the national and the multilateral levels. Switzerland consequently looks for a positive outcome to the current Doha Round negotiations.

7. Switzerland thus welcomed the *Decision adopted by the WTO General Council on 1 August 2004*, which gives fresh impetus to the Doha negotiations and lays the groundwork necessary for the next stage of negotiations on modalities. This Decision is a key step towards opening up the world economy, as WTO Members have succeeded in agreeing on the negotiating framework for non-agricultural market access (NAMA) and agriculture, furthering negotiations on services and other issues and starting negotiations on trade facilitation. Switzerland believes that, in order for the negotiations to succeed, they must be fair for all participants, whether developed or developing countries, whether large or small. In this connection, there must be sufficient transition phases for sensitive economic sectors (agriculture, for example) to allow for socially sustainable

[2] Exports and imports of goods and services amounted to 42.6% and 36.0% of GDP respectively in 2003.

structural adjustment. Switzerland nonetheless regrets the fact that the links between trade and investment, the interaction of trade and competition policy and transparency of government procurement, which were all mentioned in the Doha Declaration, are not in the negotiation programme, meaning that these issues will not be addressed in the Doha Round.

8. As to *European integration*, Switzerland began implementing the first seven bilateral agreements as from 1 June 2002. In addition, negotiations with the EU were concluded in June 2004 on a second series of bilateral agreements in such diverse fields as justice, police, asylum and migrations (under the Schengen and Dublin Agreements), the taxation of savings and action to combat fraud in indirect taxation (customs fraud) and the areas that had not been covered by the first Bilateral Agreements, in particular processed agricultural products, the environment, statistics, pensions, the media and a package of measures presented as a declaration of intent in the field of education, in-service training and youth programmes.

9. Switzerland has also continued to work at the EFTA level, expanding its network of *free-trade agreements* in the Mediterranean, South-Eastern Europe and more recently with countries outside Europe. The preferential policy followed by Switzerland and the EFTA countries does not aim to take the place of trade liberalization on the world level but to eradicate discrimination with regard to Swiss exporters which is the result of preferential agreements signed by third countries. The policy is thus complementary to Switzerland's commitment within the WTO process.

10. To date, the EFTA States have signed free-trade agreements with 13 partners: Turkey, Israel, Romania, Bulgaria, Morocco, the Palestinian Authority, Macedonia, Mexico, Croatia, Jordan, Singapore, Chile and Lebanon. In addition, Switzerland has signed bilateral free-trade agreements with the European Community and the Faroe Isles. Negotiations are currently ongoing between EFTA States and several Mediterranean countries and countries outside Europe (Tunisia, Egypt, SACU - South Africa, Botswana, Lesotho, Namibia, Swaziland – and Canada). The EU enlargement to 25 countries on 1 May 2004 brought about the simultaneous termination of free-trade agreements with eight new EU members, that is Estonia, Hungary, Latvia, Lithuania, Poland, Slovakia, Slovenia and the Czech Republic. The free-trade relations between Switzerland and these countries will be maintained under agreements with the European Union.

11. Switzerland also firmly supports the *integration of developing countries, transition countries and least developed countries in the world economy* through trade and investment. The Swiss authorities are in favour of markets being opened to products from the least developed countries (LDCs), of action to assist countries in the process of joining the WTO and of strengthened technical assistance to developing countries to integrate into the multilateral trading system and promote their capacity-building. Moreover, Switzerland has strengthened its negotiating mechanism by establishing a high-level unit whose main tasks are to analyse the trade-related needs of developing countries, and in particular the most vulnerable among them, and to incorporate sound development policy principles into trade negotiating positions.

12. In general terms, the Swiss Government is seeking to ensure the internal *consistency* of its policies by a high degree of coordination between the relevant agencies and federal offices, including in international negotiations. At the same time, the Government aims to promote the necessary external *transparency* by means of *information*, followed by the *participation* of the Swiss people, Parliament and interested parties in the *decision-making process*. In so doing it can ensure that policies command wide *support*.

13. This report first sets out the economic environment in which Swiss trade has developed since the last examination of Switzerland's trade policy, in 2000. It then presents the Swiss Government's

main objectives concerning structural adjustments to strengthen economic growth. The report also describes the main directions of reforms that have already been undertaken and of current reforms, together with the other main priorities of Swiss economic policy, at the domestic and foreign levels. Finally, it points to the objectives followed by Switzerland in multilateral negotiations, which remain an important instrument in continuing to open up the Swiss economy and integrate in the world economy, together with the necessary additions to current reforms at the domestic level.

II. ECONOMIC ENVIRONMENT

(1) ECONOMIC AND MACROECONOMIC POLICY DEVELOPMENTS

(i) Economic trends

14. In 1997, the Swiss economy began to pick up after a decade of relatively disappointing performance. After a brief slow-down in 1998, partly due to the impact of the Asian crisis, the recovery accelerated during the second half of 1999, with a growth rate of 3 per cent in comparison with the previous two quarters. This trend continued in 2000.

15. During 2001 there was the beginning of a slowdown, with share prices on the international stock markets starting to fall. In the autumn of 2001, the slowdown was more marked and a series of substantial negative shocks affected the Swiss economy. The terrorist attacks on New York and Washington, D.C., the bankruptcy of Swissair, the continued collapse of the investment bubble on financial markets, the news of accounting scandals and then the SARS (Severe Acute Respiratory Syndrome) epidemic in Asia all had a strong impact on the Swiss economy from autumn 2001. Taken as a whole, 2001 still managed to benefit from the dynamism of 2000, even though GDP began to contract during the third and fourth quarters of 2001. The shocks in 2001, added to the decrease in external demand, had their full impact in Switzerland in 2002 and 2003. In 2002, Switzerland's annual GDP was almost stagnant (+0.3 per cent) and over the whole of 2003 there was a decrease in real GDP (-0.4 per cent). In 2002 and 2003 Switzerland experienced a shrinkage in employment and an increase in unemployment. Inflation measured by consumer prices, which was already low in 2000 (1 per cent on a yearly average), fell to 0.5 per cent until 2003, reflecting the weakness of the Swiss economy during the period under review.

16. From mid-May 2003, economic activity in the Euro zone picked up, and the Swiss economy also recovered substantially, initially largely stimulated by the external sector. Driven by very positive monetary movements, economic recovery in Switzerland was strengthened during the second half of 2003 and the beginning of 2004. Mid-2004, growth was mainly stimulated by domestic demand, whereas the very dynamic expansion of exports as from the middle of 2003 suffered a setback in the summer of 2004, while still at a high level. On the job market, and contrary to expectations, the rate of unemployment reacted less rapidly to the economic upturn and employment continued to retract until the middle of 2004. Between autumn 2003 and August 2004, the unemployment rate (seasonally adjusted) stayed virtually unchanged at 3.9 per cent.[3]

(ii) Foreign trade

17. *Exports of Swiss goods*[4] increased greatly in value at the end of the 1990s until the first half of 2001. They then fell back slightly because of the global economic slowdown. It was only in the first half of 2004 that the value of exported goods was greater than that recorded in the first six months of 2001. In all, the value of exports of goods rose from 67.6 billion Swiss francs in the first half of 2001

[3] See http://www.seco.admin.ch/themen/zahlen/wirtschaft/konjunkturtendenzen/index.html?lang=fr.
[4] Excluding trade in precious metals, precious stones, works of art and antiques.

to 70.6 billion Swiss francs for the first half of 2004 (+4.5 per cent). *Imports of goods* also continuously increased in value at the end of the 1990s, peaking during the first half of 2001. Imports then fell back slightly until the second half of 2002. Since then, they have picked up a little, reaching 65.3 billion Swiss francs during the first half of 2004, while staying 3.3 per cent below their level of three years earlier. These developments mirror the general economic recession, with the marked slowdown in the equipment sector and the reduction in domestic demand that occurred near the end of 2001.

18. Exports of chemical products increased in value by about 18 per cent, while those of precision instruments by about 20 per cent between the first half of 2001 and the corresponding period of 2004. The value of exports of machinery and electronic appliances and equipment was particularly affected by the global weakness in investment demand, falling back by 13 per cent over the same period. Conversely, there was an increase of about 10 per cent in imports of chemical products in the same period. Consequently, the percentage of chemical products in imports rose to 22 per cent during the first half of 2004, with pharmaceuticals holding an increasing share of this category of products. However, there was a substantial decrease in imports of machinery and electronic appliances and equipment, with the value of imports in this sector standing 14 per cent lower in the first half of 2004 in relation to the level reached three years earlier.

19. Between the first half of 2001 and the same period of 2004, the greatest increase in exports of goods was that in goods exported to transition countries (mainly China) and the emerging Asian markets. The rate of increase in exports to the 25 EU countries, Switzerland's main trading partner with about 63 per cent of exports, was less than the average (3.6 per cent). Meanwhile, imports from the 25 EU countries fell by only 0.7 per cent, i.e. less than the average. However, imports from the United States and Japan fell substantially during the period under review, which for the United States also mirrored the strong appreciation in the dollar exchange rate which continued until 2002. The largest increases were in imports from certain EU partners (in particular the new member States) and China.[5]

(iii) Foreign direct investment flow

20. Exports of capital linked to *foreign direct investment (FDI)* came to 75 billion Swiss francs in 2000 following the dynamic global movement of mergers and acquisitions. In the following two years, the financial crisis and economic weakness weighed heavily on FDI development. Thus, in 2002 FDI outflows hardly reached about one sixth of the value recorded in 2000. In 2003, Swiss companies' capacity to invest abroad picked up thanks to the economic recovery. Above all, investments in the United States increased rapidly in 2003. On the other hand, investments in the EU decreased yet again. FDI flow into Switzerland was 33 billion Swiss francs in 2000, i.e. at a new record level. Investments in the industrial sectors, which amount to only 15 per cent of FDI in Switzerland, rose particularly sharply. During 2001 and 2002, FDI inflows nonetheless fell to 15 billion Swiss francs and 9 billion Swiss francs respectively, owing to the weakness of the world economy. In 2003, inflows increased again to 16 billion Swiss francs. The greater part of the capital came from the United States – the largest country of origin – and essentially went into the financial sector and holding companies.

(iv) Macroeconomic policies

21. Since 2000, *Swiss economic policy* has given major priority to a macroeconomic policy environment designed to maintain stability. The new *monetary policy* framework has allowed the

[5] See http://www.seco.admin.ch/themen/zahlen/wirtschaft/aussenwirtschaft/unterseite00225/index.html?lang.

Swiss National Bank (SNB) to react quickly to an international environment disturbed by a series of substantial negative shocks.[6] SNB monetary policy has been geared to ensuring price stability and balanced recovery of growth. Too strong an appreciation of the Swiss franc in relation to the Euro has thus been avoided, despite the massive adjustment of the dollar vis-à-vis the Euro that has taken place since 2002.

22. Following a decade in which *public finances* considerably worsened, during which the debt/GDP ratio increased from 30 to 55 per cent, stabilization measures aiming in particular at wiping out the structural deficit were taken at all levels in public bodies. These measures should ensure that public administration finances gradually eliminate their deficits over the medium term. At the federal level, a budgetary rule in the shape of a constitutional amendment – the debt brake[7] – should lead to a structurally balanced federal budget as from 2007. This rule has been applied since 2003, but given the existence of a large structural deficit, stabilization is gradually being achieved by authorizing a supplementary deficit of 3 billion in 2004, 2 billion in 2005 and one billion in 2006. The aim of the debt brake is to balance the budget over the medium-term, while giving free play to automatic stabilizing mechanisms. This instrument thus allows the debt level to be stabilized while reinforcing the credibility of budgetary policy without preventing an anti-cyclical budgetary policy.

(v) Economic outlook and risks

23. Between early and mid-2004, the negative *risks* for both the international and Swiss economic climate increased. The higher than expected rise in oil prices, the beginning of a dip in business leaders' confidence in the future, a halt in the increase in Swiss exports, which are nonetheless at a high level, together with the still troubling level of domestic demand in Germany, Switzerland's main trade partner (accounting for 20 per cent of Swiss exports): all constitute risk factors. The slower improvement on the Swiss job market is also indicative of uncertainty about the quality of the movement from economic upturn to domestic demand, and in particular household consumption. Nevertheless, the Swiss authorities have kept their growth forecast for Swiss GDP at 1.8 per cent for 2004 and 2.3 per cent for 2005[8] because of the international economic context, a very favourable exchange rate for the Swiss franc and interest rates, and also available economic information that points to buoyant development during the first six month of 2004. The slight acceleration in Swiss GDP expansion in 2005 presupposes similar development throughout the EU countries, with which Switzerland largely shares its vitality on the economic front.

24. In the wake of an economic performance that for long has been one of the least dynamic internationally, major *structural reform* projects have been undertaken in Switzerland in recent years, or are in preparation, with the aim of increasing competition on product markets. Still more remains to be done in order to reach the level of other countries, in particular the EU members.

(2) MAIN AIM OF THE STRUCTURAL REFORMS: TO STRENGTHEN SWISS ECONOMIC GROWTH

25. Following Switzerland's failure to join the European Economic Area (EEA) in 1992, which would have given impetus to a wide-ranging reform programme, it became clear that independent efforts had to be made for the Swiss economy, as economic fluctuations could no longer hide the structural weaknesses that had appeared after the first oil shock. Since that time, the Swiss Government's growth policy has turned towards reforms to increase productivity. During the latest session of the legislature, reforms concentrated on four growth factors: production efficiency, labour input, innovation and the impact of the State in the economy.

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[6] See http://www.snb.ch/f/geldpolitik/geldpol.html.
[7] See http://www.efd.admin.ch/f/dok/faktenblaetter/efd-schwerpunkte/106_schulden.htm.
[8] See http://www.seco.admin.ch/news/00378/index.html?lang=fr.

26. In order to improve the efficiency of the productive sector, competition has been strengthened and public infrastructures progressively liberalized. The projects that have been implemented include more particularly the revision of the Law on Cartels, the liberalization of the postal market, telecommunications, rail transport of goods (see also paragraphs 37 to 39). With regard to opening up the market to international competition, the signing of the bilateral agreements with the EU, which include *inter alia* freedom of movement, air transport and the Law on Technical Barriers to Trade, is also indicative of substantial progress (see paragraphs 70 et seq.).

27. The second growth factor involved increasing the supply and quality of labour input. To make work and family compatible, a crèche-building programme was launched and maternity insurance was approved by referendum on 26 September 2004. The revision of unemployment insurance has brought about a sustainable reduction in insurance contributions by reducing the incentive to make maximum use of benefits. The State has also continued to invest in training while improving its efficiency, partly thanks to a new Law on Vocational Training.

28. Innovation is one of the most important engines of growth in Switzerland. The relevant framework conditions have been improved by facilitating contacts between universities and economic circles, by increasing resources available for research, revising the Law on Patents and the taxation of employee options, and by modernizing the law on the largest joint stock companies.

29. Finally, the impact of the State on the economy was closely examined. The debt brake that was introduced is a mechanism for controlling State debt during the economic cycle. By analysing the impact of the regulation and carrying out tests on SMEs (small and medium-sized enterprises) it is possible to evaluate the administrative cost and indirect costs of the laws. A reform of company taxation has also made this source of fiscal revenue economically more efficient.

30. Despite the reforms undertaken, it has been clear in recent years that Switzerland's weak growth has remained a pressing problem. However, it was also necessary to take into account the result of some of the *referendums*. Thus the *reform of the electricity market*, designed to liberalize the electricity market, was rejected in the referendum in 2002. In this case, alternative solutions had to be found: the Federal Tribunal (Supreme Court) thus ruled that existing legislation on competition allowed electricity producers and consumers alike to ask for access to electricity networks. Similarly, a *financial package* that was designed to bring about a reform of direct taxation in Switzerland, in particular by reducing tax pressure on families and modifying the system of taxing property, was rejected in the referendum in May 2004, mainly because of opposition from the cantons which feared that there might be a transfer of the Confederation's excessive financial burdens to the cantons at a time when many of them are still experiencing financial difficulties.

31. Accordingly, growth policy remains a priority for the Swiss Government. Following the report on growth and the proposals made by an ad hoc working group on growth, the Federal Council approved a package of 17 measures for economic growth, as part of the programme of the 2003-2007 legislature.[9] In actual fact, the programme already contains a host of other measures that will have an impact on growth. To be considered as belonging to the growth package, each measure had nonetheless to obey three criteria. First, it should be an essential measure on the macroeconomic level (as opposed to the sectoral level, or to have no direct economic impact). Second, it should be implemented specifically by the Federal Council during the legislature and, last, it should be compatible with a lowering of State expenditure and with a market economy system. Seventeen measures were adopted, with the package divided into two halves.

[9] See http://www.evd.admin.ch/evd/news/03248/index.html?lang=fr.

32. The first half concerns the improvement of the framework conditions for the dynamic, productive and competitive part of the economy. To attain this objective means:

- Reforming company taxation to guarantee in particular greater fairness in the taxation of different legal forms and different types of capital;

- improving company management by better transparency;

- revising the Law on the Domestic Market to heighten competition between companies on this market;

- revising the Federal Law on Government Procurement in order to continue desegmenting markets that are too diverse;

- revising VAT to simplify it and to reduce distortion on investments;

- examining the need to adapt to developments in the services market, particularly in the EU; and

- cutting down on administrative burdens.

33. Secondly, the aim is to guarantee that the dynamic, productive and competitive part of the economy has access to more resources, either by increasing the supply of factors, or by limiting the use of inputs by the low-productivity part of the protected domestic sector. In this respect, the purpose is:

- To extend the free movement of persons to the new EU member States;

- to help employees aged between 55 and 67 to participate in the job market;

- to eliminate the structural deficit and stabilize State expenditure, in particular with a stabilization plan;

- to revise the Law on Health Insurance to give a greater economic orientation to the health system;

- to revise disability insurance to limit the growth of expenditure of this social insurance and to ensure that it effectively attains its objectives;

- to continue agricultural policy reforms to improve productivity in agriculture and prepare for greater international openness;

- to open up the electricity sector in such a way as will be compatible with EU directives.

34. In this context of increasing productive resources in favour of the economy, it is also planned to invest further in the system of education and reform the system to make it more productive and successful. A communication on this subject will be issued by the Federal Council on Training, Research and Technology (FRT) 2007-2011.

35. It may seem surprising that the negotiation of international agreements mentioned in the programme of the legislature are not part of the growth package. The main reason is that because of

the criterion of the Federal Council's exclusive responsibility, international negotiations have not been included in the growth package. The second reason is that the weakness in productivity growth lies above all in the domestic sectors, where there are consequently more reforms to be carried out. In fact, given the specific character of the Swiss economy (high external competitiveness, balance of payments surplus, strong Swiss franc, etc.), the reforms to stimulate productivity in domestic markets have become essential for the success of the external economy and growth in general.

III. MAIN TRACKS OF RECENT AND CURRENT STRUCTURAL REFORMS AND OTHER PRIORITIES OF SWITZERLAND'S ECONOMIC POLICY

(1) DOMESTIC POLICY AREAS

36. As indicated above, the Swiss Government has continued to implement the structural reforms undertaken in the 1990s despite the rather unfavourable economic conditions at the beginning of this century, in order to stimulate its very weak economic growth and to strengthen domestic competition, the inadequateness of which can in part be explained by very high prices when compared with other countries. In the following paragraphs can be found some of the key aspects of reforms undertaken or underway that aim to strengthen the Swiss economy's competitive capacity (revision of the Law on Cartels, liberalization of the postal market, telecommunications and rail transport of goods, revision of the Customs Law, further reforms in agriculture, revision of the Law on the National Bank and the regulation of financial services, intellectual property, government procurement, reduction of technical barriers to trade, regulating genetic engineering and products containing genetically modified organisms, simplification of administrative procedures, State trade), together with other priorities of Swiss domestic policy (environmental policy, fundamental labour standards).

(i) Structural reforms

37. With regard to *competition*, the amendment to the Law on Cartels came into force on 1 April 2004.[10] Notable among the main changes is the fact that penalties can be directly applied for certain types of infringement. Previously it was necessary to determine the unlawfulness of the restraint on competition. Since the determination did not in itself lead to penalties, it had few practical consequences for the company in question. Only in the case of a subsequent offence could administrative or criminal penalties be applied to the company at fault, something which substantially diminished the deterrent effect of the legislation. Another new element in the 2004 amendment is the introduction of a leniency programme to encourage companies to reveal cartel activities in which they have played a part. Lastly, the amendment also modified the conditions in which company mergers among the media should be notified to the competition authority.

38. As to *infrastructures*, liberalization efforts are continuing. The increased competition that followed the *liberalization of the telecommunications sector* led to a very substantial reduction in the price of fixed telephone services. However, fixed costs tend to remain higher than those in other countries. This fact encouraged the Federal Council to liberalize access to the last kilometre. The question is now being debated in Parliament. As for the *postal services*, total liberalization of parcel transport was effective as from 1 January 2004.[11]

39. The first phase of the *railway reform* began in January 1999. More particularly, companies were obliged to make a clearer separation between the transport and infrastructure sectors and to introduce open access to the network. An arbitration commission was set up to guarantee that applications were treated in a non-discriminatory manner. Open access can also be granted to foreign

[10] See http://www.evd.admin.ch/evd/dossiers/kartellgesetz/index.html?lang=fr.
[11] See http://www.uvek.admin.ch/kommunikation/post/index.html?lang=fr.

rail services, if certain conditions are fulfilled. With the entry into force of the agreement on land transport between Switzerland and the EU on 1 June 2002, open access to the network has also been granted to the EU's rail services.

40. In 2004 the Swiss Government put before Parliament a *bill* to reform the current *Swiss Customs Law*, which has been in force since 1925. This law lays down customs procedures whereas the Customs Tariffs Law sets out how customs tariffs are determined. The aim of the new bill is to further harmonize Swiss customs legislation with relevant international law, and in particular with EU law and the work of the World Customs Organization. It will help provide the Swiss economy with instruments and procedures similar to those offered to its European competitors. Moreover, the new Customs Law will create the necessary legal foundation for the customs administration, to enable the administration to carry out the missions of the modern State that go beyond customs duties, such as, for example, improving border protection to guarantee the country’s internal security. From the economic point of view, the new Customs Law seeks to maintain and even extend the stages of liberalization that were introduced into the current law after the Uruguay Round, in particular with regard to processing trade. In addition, the bill provides for liberalization of the customs warehouses regime which are an important tool for an open economy and depend largely on international trade.[12]

41. Switzerland is making great efforts to pursue the *reform of its agricultural policy*, which was begun in the early 1990s. This progressive, ongoing reform is a response to the challenges arising from the country’s determination to benefit from new export possibilities, on the one hand in order to facilitate trade in agricultural products, and on the other hand to fulfil existing and future obligations under the WTO Agreement on Agriculture. This reform, moreover, makes for an adequate response to society’s concerns about ecology, food safety and animal welfare, and to adapt the agricultural policy priorities to growing budgetary restrictions, while affording farmers the best possible conditions for continuing their work.

42. The provisions on trade in agricultural products with the EU improved when the bilateral agreement on agricultural products came into force in 2002. This agreement provides, *inter alia*, for the partial or total liberalization of trade in several agricultural products, and in particular cheese. Reciprocal commitments regarding phytosanitary and zootechnical provisions, geographical indications and marketing standards recognition also fall within the scope of this agreement.

43. As to Switzerland’s WTO commitments, the reform of agricultural policy fulfils the objectives of reducing production-related support and of liberalizing the domestic agricultural market. Direct payments decoupled from production are increasingly replacing market support. Once all the facets of the "Agricultural Policy 2007"[13] are in place, the State, leaving aside customs protection, will hardly intervene any more in the market. For example, the milk quota system will be abolished by 2009 at the latest. Agricultural reforms will nonetheless be pursued beyond the present decade. There is talk of an Agricultural Policy 2011, or possibly 2015. The current reforms will also contribute to necessary structural adjustment in a particularly vulnerable sector.

44. At the operational level, the agricultural policy reform programme (AP 2007) has the main priorities of the previous reform programme (AP 2002). The reform is still based on Article 104 of the Federal Constitution, which was adopted with a large majority by the people and the cantons on 9 June 1996. This Article sets out the tasks to be performed by agriculture and lays down the main lines of agricultural policy; it states, *inter alia*, that in a market economy context, agriculture must perform many tasks (multifunctionality) and go beyond the mere production of food products. By

[12] As the bill on customs was being debated in Parliament when this report was being written, the final decisions had not yet been taken. See FF No. 6/2004, http://www.bk.admin.ch/ch/f/ff/2004/629.pdf.

[13] See http://www.blw.admin.ch/dossiers/00091/index.html?lang=fr.

means of direct payments, the Confederation remunerates ecological and other services that agriculture provides but that do not have market value as such.

45. The new *Law on the National Bank* (*LNB*), passed by Parliament in October 2003, entered into force on 1 May 2004.[14] It clarifies the monetary policy mandate of the Swiss National Bank (SNB). It states, *inter alia*, that "the National Bank shall conduct a monetary policy in the general interest of the country. It shall ensure price stability. In so doing, it shall take into account the development of the economic situation." (Article 5, LNB). In addition, the new law stipulates that the SNB must contribute to the stability of the financial system. The new law and corresponding ordinance clarify the Bank's competence in monitoring share transaction payment systems. Thanks to this supervisory function, the SNB supports the security and efficiency of the Swiss financial market infrastructures. The SNB's supervisory activities are risk-oriented, i.e. it utilizes the means at its disposal in certain fields where the risks are particularly high.

46. Three developments in the field of *financial services* are of particular interest. Work on establishing a *Federal Financial Market Supervisory Authority (FINMA)* has moved ahead considerably. Proposals on FINMA's organisation and on supervisory instruments that are valid for all specialised fields have been put forward by a commission of experts. They were published in July 2003 with an appended draft bill. The proposals suggest that the new authority should be established under public law, have legal personality and be financed by emoluments and special supervisory taxes. The new authority is initially intended to bring together the Swiss Federal Banking Commission (SFBC) and the Federal Office for Private Insurance (BPV). In August 2004, the commission of experts completed its draft bill on supervising financial markets with a section on the system of penalties, setting out the range of penalties that the future FINMA should have at its disposal.[15]

47. In the action to combat money laundering, mention should be made of the work on the *implementation of the 40 Revised Recommendations of the Financial Action Task Force on Money Laundering (FATF).*[16] Current Swiss legislation is already substantially compatible with the new standards, but some adaptations must nonetheless be made, in particular in criminal law and joint-stock company law – by including in the list of offences those deemed to lead to money laundering. At the same time, some changes must be made to the Money Laundering Law (LBA) which have proved necessary during the first years of implementation. An interdepartmental study group has been set up with the task of putting together a draft on the requisite changes in legislation to implement the FATF's 40 Revised Recommendations.

48. The third reform project that deserves mention is the *complete overhaul of the Law on Mutual Funds (LFP*).[17] The aim is partly to guarantee the euro-compatibility of the law, and partly to extend the law's scope and liberalize the field more generally, while maintaining effective investor protection. An expert committee has drafted a bill[18] accompanied by an explanatory report. The committee proposes that the law on mutual funds be completely rethought; in the future, new legal forms of collective capital investments will be introduced and all the forms of collective investments that are

[14] See http://www.snb.ch/f/snb/index.html?file=recht/content_recht.html.

[15] For further information on current reform projects of Swiss financial market regulation, see http://www.finweb.admin.ch/f/index.htm.

[16] In June 2003, the Financial Action Task Force on Money Laundering (FATF) revised its 40 recommendations, which serve as the international standard to combat money laundering and the financing of terrorism.

[17] See http://www.finweb.admin.ch/pdf_neue_Version/PDF-f/FS-Anlagefondsgesetz_EBK_f.pdf.

[18] In order to take into account the new scope, the Law on mutual funds should in the future be called "Federal Law on Collective Capital Investments (LPCC)".

recognized by Swiss law and are not subject to authorization will be governed by one single supervisory law. In order not to weaken the position of the Swiss mutual fund sector in the EU before the law is completely overhauled, the Ordinance on Mutual Funds has been partially revised.[19] This essentially concerns the implementation of the Directive on Products, the adaptation to the Directive on Services in relation to Equity Capital requirements and the introduction of a simplified prospectus for share funds. The partial revision of the Ordinance on Mutual Funds came into force on 1 August 2004. A complete revision of the Ordinance on Mutual Funds is currently being prepared and should come into force in January 2006.

49. The Swiss Government attaches paramount importance to the protection of *intellectual property* with a view to constantly promoting research, development and innovation efforts in the corporate sector. Strong protection within a strict international framework can alone justify enormous research costs in a number of sectors concerned, *inter alia,* with the life sciences. The protection of geographical indications is also essential for both agricultural and manufactured products. Consequently, recognition and international respect for geographical indications is a priority for Switzerland, in order to encourage producers to concentrate on the production of specialities.

50. In regard to intellectual property, Switzerland affords protection over and above the minimum standards provided for in the TRIPS Agreement. Three laws governing intellectual property rights – the Federal Law on Copyright and Neighbouring Rights, the Law on Patents, and the Law on the Protection of New Varieties of Plants – are currently being part revised. The purpose is to adapt Swiss legislation to international intellectual property rules. On 1 January 2002, the new Federal Law on Design Protection came into force, replacing the old Law on Industrial Designs and Models dating from 30 March 1900.[20] The main aim of this new law was, *inter alia*, to adapt Swiss law with a view to ratifying the Geneva Act of the Hague Agreement Concerning the International Registration of Industrial Designs, adopted on 2 July 1999.[21]

51. The law on *government procurement* regulates an important sector of the Swiss economy. The overall expenditure of the communes, cantons and the Confederation for the construction, supplies and services markets is close to 30 billion Swiss francs, a figure that represents about 25 per cent of total public expenditure and 8 per cent of gross domestic product.

52. Under the WTO Agreement on Government Procurement, which has been in force since 1 January 1996, the Confederation and cantons, together with public companies operating in the water, urban transportation and energy sectors, obey the WTO rules on market tenders and procurement transactions for goods, services and construction contracts, provided the contracts are above a certain threshold. Switzerland and the EU have signed a bilateral agreement that enlarges this scope. Thus, since June 2002, for Switzerland and the EU, purchases by communes, by rail transport and private companies that are concessionaires or work on the basis of special or exclusive rights, are reciprocally open on the basis of the WTO rules.[22]

53. Overall, since 1996 Swiss legislation on government procurement has proved its worth. However, the Confederation today considers it necessary to modify certain provisions that make for cumbersome procedures, complicate management or impede the use of new technical facilities. The Confederation seeks, *inter alia*, to examine whether it is possible to broaden the dialogue between the various parties involved in government procurement. Adjudication rules should be made more

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[19] See http://www.finweb.admin.ch/pdf_neue_Version/PDF-f/FS-TeilrevAnlagefondsV_EBK_f.pdf.

[20] See http://www.admin.ch/ch/f/rs/c232_12.html.

[21] See http://www.bk.admin.ch/ch/f/rs/12/0_232_121_4/index.html.

[22] See http://www.beschaffung.admin.ch/de/beschaffungswesen_bund/recht_org_zahlen/ivoeb_172.056.5.de.pdf.

flexible so that procedures can be quicker and more efficient. It is also essential to harmonize requirements at the national level. Hence, a review of federal legislation on government procurement is underway.[23] The new federal legislation should be completed by 2007, and it will have an impact on the corresponding legislation at the level of the cantons.

54. Swiss policy on *technical barriers to trade* continues to adapt national technical requirements so as not to create technical barriers to trade, and to make them compatible with those of its main trading partners. Moreover, subject to certain conditions and independently, Switzerland recognizes test reports or conformity certificates issued by foreign agencies. These efforts go hand in hand with the negotiation of mutual recognition agreements in this field.

55. Since 2000, *(public) technical regulations* and *(private) standards* have gradually continued to be aligned on those of the EU. Thus a bilateral Agreement on mutual recognition of results of conformity assessment came into force on 1 June 2002 under Bilateral Agreements I between Switzerland and the EU. This Agreement, which establishes mutual recognition of the proof of conformity, should significantly facilitate trade with EU partners. MFN-based trade should also benefit, as more products that are approved for sale in the EU can now be put on sale in Switzerland without requiring a new conformity assessment.

56. The Swiss Government's desire for reform can also be seen in the way the regulatory framework has been modified for *building* products and *control of medicines*. In the past, technical regulatory measures could be specified for certain products at a sub-federal (usually cantonal) level. For building, until 2001 competences for regulations governing products was shared between the Confederation and cantons. On 1 January 2001, the Federal Law on the Circulation of Building Products[24] and its implementing Ordinance came into force. This federal legislation unified the 26 different legislations that had been applied up to that date.

57. When the Federal Therapeutic Goods Law came into force in 2001[25], regulatory competence was transferred from the cantonal to the federal level for all pharmaceuticals for human and veterinary use, and also for medical equipment. All pharmaceuticals (on prescription or over the counter) must now be approved and recorded by the Swiss Therapeutic Goods Agency (Swissmedic) before being put on sale in Switzerland. Since the legislation on building products and therapeutic goods came into force, technical regulation falls entirely within the competence of the Confederation, with the consequent reduction in technical barriers to trade in these fields. It must, however, be said that in many fields the cantons are still responsible for market implementation and surveillance.

58. With regard to the *simplification of administrative procedures*, it should be noted that a Federal Administrative Court has been established to replace 36 Federal Appeal Commissions and departmental appeal services, which will be brought together in a single independent legal authority employing some 400 people. It will be operational in 2007, provided that Parliament is able to finish the necessary legislative work by that date. In the early years it will be housed in temporary premises in the Berne region before setting up in St. Gall, in principle in 2010.

59. Following two referendums in 1992 and 1998, Switzerland adopted a regulatory framework for *genetic engineering* and *products containing genetically modified organisms* (GMOs). It has developed a strategy based on information, safety, use of precautionary measures, consideration of

[23] See http://www.bbl.admin.ch/fr/aktuell/pressem/2004/2004_9_01_beschaffungsrecht.htm.
[24] *Loi sur les produits de construction*, LPCo – RS 933.0, see http://www.admin.ch/ch/f/rs/9/933.0.fr.pdf.
[25] *Loi fédérale sur les produits thérapeutiques* – LPTh, RS 812.21, see http://www.admin.ch/ch/f/rs/8/812.21.fr.pdf.

ethical arguments, forward-looking regulation open to future developments and respect for international rules.

60. Switzerland has recently legislated on the *use of genetically modified organisms in food*. The Federal Law on the Application of Genetic Engineering to the non-human field that regulates the use of GMOs in food production came into force on 1 January 2004. The law was notified to the WTO.[26] Requirements for the labelling of foodstuffs and animal feed containing GMOs will be amended to take into account the new Law Relating to Non-human Gene Technology (Gene Technology Law). These amendments should come into force on 1 February 2005.[27]

61. In the notification on *State Trading Enterprises* that Switzerland made to the WTO in June 2004[28], the only body included was the Swiss Alcohol Board, which the Swiss Government justified by its aim of limiting high-degree alcohol production and consumption for public health reasons. The other legislation, which dated from 1959 and whereby the Confederation had exclusive rights to importing bread flour for food safety and to protect the national flour-milling industry, was abolished in 2001. With the sole exception of the Swiss Alcohol Board, Switzerland no longer has any State Trading Enterprises in the agricultural sector.

(ii) Other domestic policy priorities

62. Switzerland is actively taking part in all international negotiations on the *environment*, to promote sustainable development throughout the world. The relevant legal basis for its participation is Article 2, 54 of the Swiss Constitution and the Federal Law on the Protection of the Environment as the principal legislation on environmental protection in Switzerland, together with Federal Council reports on foreign policy (1993 and 2000). Switzerland believes that, within the framework of multilateral environmental agreements, the use of trade-related measures which are both non-discriminatory and non-protectionist, is in certain circumstances the best way of ensuring that environmental objectives will be met. The Swiss Agency for the Environment, Forests and Landscape (OFEFP) is mainly responsible for applying the regulations on the environment.[29]

63. At the international level, Switzerland's goal is for environmental agreements to be negotiated and implemented coherently, while taking into account international trade obligations. Switzerland cooperates with foreign governments to ensure conformity with the laws on importing and exporting material that may pose a risk to human health or the environment, including hazardous waste, toxic chemical products, biocides and substances that destroy the ozone layer.

64. Switzerland has ratified all the multilateral agreements on the environment – the Montreal Protocol on Substances that Destroy the Ozone Layer, the Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and their Disposal, the Rotterdam Convention on the Prior Informed Consent Procedure for Certain Hazardous Chemicals and Pesticides in International Trade (PIC), the Stockholm Convention on Persistent Organic Pollutants (POP), and the Cartagena Protocol on Biosafety to the Convention on Biological Diversity. Implementation is ongoing. In addition, the Kyoto Protocol was ratified by Switzerland in the summer of 2003. Switzerland has thus made a commitment to reduce its emissions of six greenhouse gasses to 8 per cent below the 1990 level. The mainstay of Switzerland's climate policy is the Law on CO_2 which has been in force since 2000. In order to reach its objective of reducing consumption of fossil fuel

[26] Notifications G/TBT/Notif.00/49 and G/TBT/Notif.00/49/Add.1.
[27] Notifications G/TBT/N/CHE/40, G/TBT/N/CHE/42 and G/SPS/N/CHE/37, G/SPS/N/CHE/38.
[28] Notification G/STR/N/10/CH of 30 June 2004.
[29] See http://www.environnement-suisse.ch/buwal/fr/medien/index.html.

(overall -10 per cent, for combustibles -15 per cent and for fuel -8 per cent) stipulated in the Law, the Federal Council decided to introduce a tax incentive.

65. Switzerland also seeks to ensure that the international processes tied in with the environment in such forums as the World Summit on Sustainable Development, the Commission on Sustainable Development (CSD), the UN Forum on Forests or the Task Force for the Environment (post-Kiev process) are taken into account in ongoing environmental negotiations and consequently considered as part of the global environmental system.

66. Environmental policy is also affected by several modifications to legislation that have been enacted in *road transport* further to the Agreement signed with the EU on land transport (Bilateral Agreements I, see also paragraph 70 below). The changes include an increase to 40 tons maximum weight for lorries driven in Switzerland and an increase in the quota of 40 ton lorries from the EU allowed into Switzerland in compensation for the increase in the heavy goods vehicles tax, which is designed to encourage the transfer of goods traffic from road to rail.

67. Switzerland has spoken in the WTO about the importance of *core labour standards*. Switzerland called for the topics of trade on the one hand and social issues on the other hand to be dealt with cohesively (Singapore Consensus, confirmed at Doha in 2001). Switzerland also made clear that the WTO must deal with trade and not address the question of human rights in an independent fashion. Thus, like other international organizations (IOs), the WTO must stay within its brief while ensuring that the provisions developed within the WTO are consistent with those developed in other IOs, and vice-versa.[30]

68. Switzerland has recognized the importance of the report of the World Commission on the Social Dimension of Globalization, published under the aegis of the *International Labour Organization (ILO)* in February 2004. The social dimension of globalization is an important priority for Switzerland and is part of the follow-up to the Copenhagen Social Summit and the Millennium Summit. More particularly, the follow-up must be integrated in the multilateral system and based on the recommendation of the World Commission on the Social Dimension of Globalization report. Switzerland endorses the following recommendations in the report: integrating economic, social and environmental aspects in national and international development policies; giving priority to global growth, investment and job creation, market liberalization by means of fair rules, the prime responsibility of States, the promotion of human rights and democracy, and greater democracy within financial and trade institutions. Switzerland would look favourably on a more in-depth analysis of initiatives to progressively set out integrated policy proposals which, in given areas, would establish a fair balance between the economic, the social and the environmental fields. The first initiative could address the question of global growth, investment and job creation and the relevant bodies of the United Nations, World Bank, IMF, WTO and ILO should take part. Moreover, Switzerland would also be in favour of examining other initiatives such as organizing "Multi-Stakeholder Policy Development Dialogues" or setting up a "Globalization Policy Forum". Implementing the social dimension of globalization is also a priority for Switzerland within the framework of the 59th session of the UN General Assembly. The two co-chairpersons of the World Commission on the Social Dimension of Globalization have, *inter alia*, stated that within the framework of the General Assembly they intend to encourage a resolution asking all UN Member States, organizations and bodies, including ECOSOC, together with other relevant parties (in particular the Bretton Woods institutions and the WTO) to examine the report of the Working Party and submit their views during the 60th session of the General Assembly, in 2005.

[30] See http://www.seco.admin.ch/themen/arbeit/seiten/00067/index.html?lang=fr.

(2) FOREIGN POLICY AREAS

69. Switzerland's concern to mutually reinforce the policies of reform, liberalization and openness can also be found in the various foreign policy measures taken by the Government over the period under review.

(i) Relations between Switzerland and the EU

70. Switzerland has close relations with the EU in the matter of *European integration*. Contractually, this has meant the following. In 1972, the two parties signed a free trade agreement (for industrial products). In 1999, seven Bilateral Agreements were signed on free movement of persons, land and transport, air transport, agriculture, research, technical barriers to trade and government procurement. The Agreements came into force on 1 June 2002, enabling Switzerland not only to further open up its economy and improve its access to the EU market as an enhancement to the 1972 free trade agreement, but also to strengthen the "euro-compatibility" of the technical rules governing national economic legislation. The experience of the first two years since their entry into force is promising.

71. In the course of 2004, Switzerland has reached agreement with the EU on nine additional agreements in order to strengthen its regional links with its main economic partner.[31] These new agreements deal with cooperation in the fields of justice, asylum and migration (Schengen/Dublin), taxation of savings, action to combat fraud, processed agricultural products, the environment, statistics, the media, pensions, education, vocational training and youth. They underscore the continuation of the bilateral approach adopted by Switzerland after the rejection of membership of the European Economic Area (EEA) in 1992. The different agreements still have to be approved by Parliament, and in the possible event of a referendum, by the population.[32]

72. During the second part of the current legislature (2003-2007), the Federal Council will publishing a report on the advantages and disadvantages of Switzerland joining the EU. A wide-ranging debate will ensue on the basis of this report. The Federal Council should then be able to lay down the major guidelines of its policy towards the EU for the years ahead.

(ii) Free-trade agreements

73. In regard to *free trade*, Switzerland and its EFTA partners are seeking to extend their network of agreements. For Switzerland, an important objective is to ensure that the conditions of access to foreign markets for its exporters are equivalent to those for their competitors. Often, the only possible way of eliminating discrimination against Swiss exports – which is the result of preferential agreements concluded with third countries – is to sign free trade agreements. The preferential policy followed by Switzerland and the EFTA countries is not intended to replace trade liberalization at the global level. It is complementary to Switzerland's commitment in the WTO process.

74. The growing trend throughout the world to sign preferential regional and supraregional agreements is continuing. Consequently, the EFTA countries, including Switzerland, will carry on broadening their network of free trade agreements. EFTA State agreements include an increasing number of fields beyond trade in goods and protection of intellectual property, such as trade in services, investments and government procurement.

[31] During the first two quarters of 2004, 63.3 per cent of Swiss exports and 83.4 per cent of Swiss imports were with the EU(25).

[32] Bilateral Agreements II – Official texts, see http://www.europa.admin.ch/nbv/off/f/index.htm.

75. At the present time, the EFTA States have signed free trade agreements with 13 partners: Turkey, Israel, Romania, Bulgaria, Morocco, the Palestinian Authority, Macedonia, Mexico, Croatia, Jordan, Singapore, Chile and Lebanon. In addition, Switzerland has signed bilateral free trade agreements with the European Community and the Faroe Islands.

76. EU enlargement to 25 countries on 1 May 2004 brought about the simultaneous termination of free trade agreements with eight new EU members, namely Estonia, Hungary, Latvia, Lithuania, Poland, Slovakia, Slovenia and the Czech Republic. The free-trade relations between Switzerland and these countries will nonetheless be maintained on the basis of the free trade agreement with the European Union signed in 1972 and other relevant bilateral agreements.

77. Negotiations are currently underway between the EFTA States and Tunisia, Egypt, the SACU (South Africa, Botswana, Lesotho, Namibia, Swaziland) and Canada. The possibility of negotiating free-trade agreements with South Korea and Thailand is currently being explored. The EFTA States have signed Declarations of Cooperation with Albania, Algeria, the Gulf Cooperation Council, Mercosur, Serbia and Montenegro and Ukraine. In addition, Switzerland and the EFTA States are closely following the situation with regard to other potential free-trade partners.

(iii) EFTA/Stockholm Convention internal relations

78. An agreement amending the Convention establishing EFTA (the Stockholm Convention of 1960) was signed in Vaduz on 21 June 2001 and entered into force on 1 June 2002. Under this agreement, the level of cooperation between Switzerland and the other EFTA States is now comparable to that between Switzerland and the EU through the sectoral bilateral agreements of 1999 (with the exception of the agreement on scientific research). In addition, the Convention is supplemented by provisions covering, *inter alia*, services, movements of capital and the protection of intellectual property rights.

(iv) Cooperation with developing and transition countries

79. Switzerland, which was one of the first contributors to launch *trade cooperation programmes*, for example through the Agency for International Trade Information and Cooperation (AITIC)[33], is in a favourable position to meet the Doha commitments. The Swiss response to the work programme, which places the needs of developing counties at the core of negotiations, is that of a *trade policy consistent with development policy*, which both influences its position in the negotiation of multilateral and bilateral trade agreements and the trade part of its technical cooperation programme. To this end, Switzerland has strengthened and better targeted its existing trade cooperation – trade policy, trade efficiency, market access, trade-related environmental and social issues, basic agricultural products – while broadening cooperation to include new topics (intellectual property, transparency in government procurement, promotion of competition, standards). But Switzerland has above all established a *body to examine the consistency of these two policies*. It is an interdepartmental group whose main tasks are to analyse trade demand in developing countries, in particular the most vulnerable, and to integrate the principle of good development policy into trade negotiation positions.

[33] AITIC's brief is to help the less privileged developing or transition countries to participate more actively in the WTO's work and negotiations. It gives personalised assistance on international trade issues, and specific information on subjects that are of direct interest to the less privileged countries. Its services are also intended for countries that do not have a Mission in Geneva.

(a) Cooperation in trade policy

80. Switzerland has deliberately endeavoured to bring its work programme closer to the challenges put forward in the Doha Work Programme. To this end, it is working at both the multilateral and bilateral levels.

81. To *strengthen national capacity-building in trade policy in partner countries*, the Swiss Government has broadened its field of action, in particular in the fields of intellectual property, transparency in government procurement, competition law and standards. These complex areas, which have taken on particular importance since the Doha meeting, today make up a major challenge for developing countries (for example, the trade in biological resources that Switzerland supports through the UNCTAD Biotrade initiative, and also thanks to bilateral projects). A thematic approach should allow far in-depth involvement to help the countries in question formulate their trade policies and implement the necessary reforms. Such an approach entails the participation of not only governmental bodies, but also the private sector, civil society and academia. In this respect, a pilot project to set up a Trade Law Centre in southern Africa has been implemented. Depending on results and possibilities, this kind of project could be implemented in other regions and be of greater benefit to LDCs.

82. Another example is the *exports promotion*, which necessarily goes hand in hand with the developed countries' market access demands in the Doha Declaration. Developing countries face internal restrictions on trade that give rise to high transaction costs, and consequently diminish their competitiveness on the world market. Swiss economic cooperation measures aim on the one hand to create internal framework-conditions that are more suitable for trade, and on the other, to reduce the cost of transactions and hence improve the competitiveness, particularly of SMEs, on the international market. Three levels of measures are envisaged: improving framework-conditions for trade (by supporting reforms of customs administrations or by backing the setting up of independent services for certification, accreditation and control, for example sanitary and phytosanitary conditions of products for farming), support for trade associations, strengthening export capacity and developing electronic commerce.

83. Switzerland has also strengthened its *programme on horizontal themes* such as advice and expertise for government officials responsible for foreign trade issues in a number of partner countries. Special emphasis is laid on accession procedures, implementing WTO rules, negotiations and regional trade integration. For countries that are already Members, Switzerland is continuing its support for the Integrated Framework multilateral initiative, which seeks to integrate the trade component in national poverty reduction plans and strengthen national trade policy capacities in a coordinated way.

84. Switzerland disburses roughly 40 million Swiss francs a year on its trade cooperation programmes.

(b) Trade policy consistent with development policy

85. The aim of Swiss economic cooperation is the *progressive integration of developing countries, particularly the least developed, within the global trading system*. To better pursue this objective, Switzerland is continuing to revise its system of preferential tariffs while keeping in sight the aims of its agricultural policy.[34] Given the difficulties met by developing countries, and

[34] The second of three stages in the system of preferences – zero tariffs, zero quotas – for LDCs, came into force on 1 April 2004 and reduced tariffs by 55 per cent to 75 per cent in relation to the normal rate. The third stage will be submitted to Parliament in 2006.

particularly the LDCs, through the erosion of preferences and the rules of origin framework, the Swiss Government is considering whether it is desirable to target its system of preferences more efficiently on countries whose economic competitiveness depends on the system, to reform the rules of origin and to promote multilateral "best practices" with regard to systems of preferences.

86. Such a view of *trade policy* is *consistent* with *development policy*. Similarly, the Swiss Government closely follows the impact of its negotiating positions on the economic development of developing countries. *Trade and development* are not necessarily antagonistic. Some policies are neutral; others are more favourable to development, but do not for all that impinge on trade interests (for example, encouraging progressive yet ambitious liberalization of the temporary movement of persons for the supply of services). There are, however, fields where trade and development interests conflict. In these cases, Switzerland tries to find alternatives that will diminish these conflicting effects. Since, for example, the Swiss agricultural reform programme does not allow for a rapid opening up of the market, Switzerland has made priority commitments to reduce export subsidies, to provide food aid that is not motivated by a desire to eliminate agricultural surpluses and to substantially cut back tariff escalation in the food industry. To this end, Switzerland has ordered internal studies to take a critical look at the existence of tariff escalation and peaks together with quota administration methods and their potential impact on developing countries' exports. These studies, once examined and discussed, will help Switzerland to fine-tune its negotiating position.

87. Again, from the stand point of consistency, Switzerland is seeking innovative solutions in order to propose a tariff reduction package for industrial products that takes account of a WTO Member's trade level and development potential. Moreover, Switzerland is looking into ways of off setting the difficulties that developing countries experience in responding to new disciplines in trade facilitation by linking these efforts to increased specific technical assistance.

88. Another key matter of thought is the question of *special and differential treatment (S&D)*, where Switzerland is trying to introduce a more systemic approach to the question in discussions at the WTO. The aim is to target more efficiently this favourable treatment of development for countries with the greatest needs, for example by developing criteria that take account of the level of development in S&D. In addition, Switzerland is proposing a mechanism to accompany the transition to accession to special agreements. This would be a monitoring activity to support countries as they set up the necessary institutions. This means, *inter alia*, that together with the authorities, technical missions would periodically examine the quality and efficiency of the technical assistance provided, and also the measures taken at the national level. The date on which obligations came into force would be determined by validation by the Members of the organization, in consultation with the country in question.

89. The work on consistency will cover an *extended period of time*. It is a slow and difficult process that presupposes official support of the government in question. After two years of experience, Switzerland stands ready to pursue its commitment to consistency.

(v) Customs measures

90. As for customs registration, documentation and procedures, two measures have been taken since 2000. First, in accordance with its obligations under the Harmonized System Convention, Switzerland implemented the HS 2002 changes on 1 January 2002 and submitted its amended Schedule of Concessions to the WTO for verification and certification. Second, more substantial reductions and simplifications were introduced by the adoption of two ordinances on 1 March 2002: one from the Federal Council dealing with reductions in duties on passenger traffic (Ordinance on passenger traffic) and the other from the Federal Department of Finances on the tariff rate for

passenger traffic. The most significant simplification is the application of a single exemption of 300 Swiss francs per person per day on all goods, with the exception of alcoholic beverages and manufactured tobacco subject to specific quantitative exemptions franchises, and also imported agricultural products subject to quotas and in quantities liable to customs duties. With this modification, the distinction between border traffic and passenger traffic has disappeared. Thus the passenger's place of domicile no longer plays a part in the granting of value exemptions and quantitative exemptions.

(vi) Rules and disciplines

91. In multilateral forums, Switzerland constantly seeks the adaptation of *rules* and *disciplines* to enable governments to respond to the challenges of globalization. This is what lies behind Switzerland’s efforts regarding a round of multilateral negotiations with a sufficiently broad negotiating programme to satisfy all 148 WTO Members.

92. Switzerland adopted the same position in the steel dispute with the United States, when for the first time Switzerland took part in a WTO panel as a complainant and in an Appellate Body proceeding (WT/DS253/AB/R). With the seven other co-complainants, Switzerland successfully challenged American safeguard measures which, in the shape of supplementary tariffs of up to 30 per cent, had been imposed on 10 groups of steel products on 20 March 2002. One week before the WTO Dispute Settlement Body adopted the report by the Appellate Body, on 4 December 2003, the United States terminated the measures which were found to be inconsistent with Article XIX of GATT 1994 and the Agreement on Safeguards.

(vii) Exports promotion

93. Established under a Federal Law on Export Risk Guarantees, the Swiss Export Risk Guarantee Scheme (GRE) aims to create and safeguard employment opportunities in Switzerland, while promoting foreign trade through, *inter alia*, the diversification of export markets. The GRE covers political and transfer risks, trade risks and pre-delivery risks. Until recently, only trade risks could be covered when buyers were State or parastatal buyers, equally when public services were involved. Private sector trade risks, on the other hand, could be covered only if a GRE-approved bank provided a guarantee. Although the Swiss authorities are still of the opinion that trade risk coverage should be left to market players, they had to face the fact most other industrialized countries had included coverage of these risks in their export risk guarantee schemes. This development was also the outcome of a growing trend to privatize activities previously controlled by the public sector, both in developing countries and in transition countries. To avoid Swiss export companies from being systematically placed at a disadvantage in relation to foreign competitors, new legislation was prepared, *inter alia*, to extend GRE coverage to private buyers. It was accepted in a referendum in 2004 and is currently before Parliament.[35]

94. Lastly, in 2000 a legislative amendment was designed to improve export opportunities for the official export promoter (Osec Business Network Switzerland) to develop SMEs' export capacity. By providing information, advice and contacts, Osec answers the specific needs of SMEs, which, because they are small, are not always able themselves to seek out all the necessary information on potential markets. Osec's activities were once again debated in Parliament in 2003. The discussion centred on the risk of violating the principle of subsidiarity *vis à vis* private sector supply that applies to all of

[35] See http://www.seco.admin.ch/imperia/md/content/publikationenundformulare/lasre_fr.pdf?PHPSESSID=31cf0f3e621606969def6a1a2ea46251.

Osec's services through competition between Osec and private sector suppliers.[36] Another related issue was the risk of cross-subsidization between Osec's government-subsidized services (required by law) and its own private sector services (allowed by law).

IV. SWISS POSITION IN THE DOHA MULTILATERAL TRADE NEGOTIATION ROUND

(1) GENERAL APPROACH TO TRADE POLICY

95. A policy of openness and progressive liberalization of foreign trade make up the other facet of the Swiss Government's endeavours in structural reforms to strengthen economic growth. This openness is a welcome development opportunity for the most dynamic economic sectors. The resulting additional economic growth also tends to facilitate the necessary structural adjustments which would prove to be even more difficult in less favourable economic conditions. Traditionally, in industry and many services, Switzerland has applied a policy of openness. Economic performance in these sectors and the standard of living reached show that this policy has generally been a success. Competitiveness on foreign markets, however, is never acquired once and for all. The moves to openness and liberalization should therefore be kept up. At the same time, for the other, more vulnerable sectors of the economy, the necessary openness and liberalization must occur at an acceptable pace. Hence, a sector-specific approach is needed.

96. The trend towards faster globalization that stems from increased interdependence includes both opportunities and challenges for all parties involved in international trade. For opportunities to gain the upper hand, the progressive liberalization of trade must be controlled by international rules that are correctly applied by all. This is particularly important for small countries which are often more vulnerable because of their strong dependence on foreign trade. Switzerland is no exception. Consequently, this means increasing multilateral cooperation and strengthening its institutions. In this connection, the Swiss Government believes that a key role must be assigned to the WTO in the fields of the progressive liberalization of international trade, the establishment of rules, rights and obligations governing international trade, and also the settlement of disputes. It is also necessary to strengthen the world trading system by better integration of developing countries, transition countries and the LDCs.

97. In view of the historical importance of international trade in the development of the Swiss economy, the Swiss Government is strongly attached to an open system of multilateral trade. If Switzerland also participates in various bilateral or regional free-trade agreements, it is because the Government regards such agreements as a further means of speeding-up trade liberalization at the international level. On the other hand, they can in no sense act as a substitute for the multilateral trading system. Faced with the growing trend towards regionalization of trade, the Swiss Government believes that strengthening the multilateral trading system is a priority.

(2) SWITZERLAND AND THE DOHA DEVELOPMENT AGENDA

98. The Swiss Government intends to maintain active support for further multilateral trade negotiations within the framework of the Doha Development Agenda. The negotiations should not only cover market access but should also aim at strengthening existing trade rules and introducing new ones, promoting consistency between the multilateral trading system and other policies such as the environment or development. Given the importance that it attaches to a favourable outcome to

[36] *Rapport sur la politique économique extérieure 2003* and *Message concernant des accords économiques internationaux du 14 janvier 2004*. See http://www.admin.ch/ch/f/ff/2004/257.pdf.

these negotiations, the Swiss Government has clearly defined its objectives for each of the negotiations specific to the Doha Round, which can be summarized as follows:

99. With regard to *non-agricultural market access*, the Swiss Government seeks to obtain better access to other markets (*inter alia* to those of emerging countries outside Europe with which Switzerland does not have a free-trade agreement). The Swiss Government believes that an ambitious formula supplemented by sectoral policies and negotiations on non-tariff barriers should be developed on the basis of the framework agreement of 1 August 2004.

100. Regarding *services*, Switzerland has given full backing to improving market access; its initial offer was submitted in April 2003 and covers horizontal commitments, professional services, postal services, telecommunications services, construction-related services, education services, tourism services, and sea, air and road transport services. The Federal Council has confirmed its commitment to apply the principle of no a priori exclusion of any sector or mode in the GATS negotiations. Consequently Switzerland is examining all the requests it has been received. Particular attention is given to requests that are in line with its growth policy and the possibilities of increasing market access and national treatment. As for public services, Switzerland does not make commitments that are incompatible with its current federal and cantonal legislations. The Swiss Government's requests to other Members mainly concentrate on sophisticated high added-value services and on services that are used as inputs by other companies. Its requests also fully take into account Members' market size and levels of development. The Swiss Government defends uninterrupted negotiations in high-quality services. It intends, moreover, to submit a revised offer in May 2005.

101. Switzerland has a systemic interest in the *strengthening of WTO rules*. It takes the view that rules should be regularly updated to take account of developments in the world economy. Moreover, any inconsistencies between the various rules in force should be examined. As to the rules currently being negotiated, it should be stressed that Switzerland neither applies anti-dumping duties nor countervailing measures. It is, however, in favour of strengthening the rules in these fields in order to prevent the abusive effects of such measures. Switzerland also calls for clarification of the rules on customs unions and free-trade agreements in order to increase security and transparency and ensure compatibility and reciprocal support between regional trade agreements and the multilateral trading system.

102. As regards the "*Singapore issues*", Switzerland is gratified that, when the Decision was taken by the General Council on 1 August 2004, it was decided to launch negotiations on *trade facilitation*, which represents a key demand for Swiss economic players. Switzerland expects simplified streamlined customs procedures. Substantial gains in efficiency should be achieved by reduced transaction costs which would be of benefit to all economies. Switzerland nonetheless regrets that the relationship *between trade and investment*, the *interaction between trade and competition policy* and the *transparency in government procurement*, mentioned respectively in paragraphs 20 to 22, 23 to 25 and 26 respectively of the Doha Declaration, are not part of the negotiating agenda. Switzerland intends to take firm steps so that these topics continue to be examined within the WTO framework, even if not within the Doha negotiations. Otherwise, the WTO could well become obsolete if it does not manage to follow the rapid development of trade and investment in the world economy.

103. As for *agriculture*, Switzerland intends to pursue the reforms of its agricultural policy (see paras. 41 to 44). Like the other G10 members, it is seeking an agreement which, as well as continuing with progressive liberalization of market access, a gradual reduction of domestic support – a source of trade distortions – and the elimination of all instruments with an export-subsidy effect, also takes account of the non-trade related aspects of agriculture. These are food security, protection of the environment and the countryside, animal welfare, consumer information on production methods and

the protection of geographical indications. The liberalization process brings about additional economic pressures for farmers in the G10 countries. For this reason, Switzerland calls for the modalities to hasten reforms that can be maintained and allow sufficient flexibility. In this regard, it is gratifying that WTO Members have explicitly recognized in the negotiations the need to take account of sensitive products.

104. In the case of *geographical indications*, the Swiss Government is looking to extend the additional protection that the TRIPS Agreement currently reserves only for wines and spirits to all products (agricultural and industrial), together with the creation of a multilateral register for wines and spirits, with legal effect.

105. In the field of *trade and environment*, Switzerland has over these past four years actively participated in the work of the WTO Committee on Trade and Environment in Special Session (CTESS) and in that of the Committee on Trade and Environment (CTE) by submitting several documents on the issues under consideration. One of Switzerland's priorities has been to clarify the link between the WTO provisions and the multilateral agreements on the environment, so as to ensure consistency between the two systems in the event of a dispute. In addition, Switzerland aims to achieve more favourable treatment of environmental goods.

106. Switzerland is actively taking part in negotiations designed to improve the *dispute settlement mechanism*. This mechanism is of particular interest to the smaller WTO Members, and constitutes a guarantee that the law prevails over strength and an assurance that the commitments undertaken will be fulfilled. An improvement of these rules is thus of major systemic interest to Switzerland.

107. With regard to *special and differential treatment (S&D)*, Switzerland believes that S&D dispositions should be better adapted to the needs of specific groups of developing countries: the least developed countries and countries with similar economic structures should gain greater benefit than more advanced developing countries. To this end, and to make the system both transparent and predictable, a system of objective and relevant criteria from the trade point of view should be developed. In addition, a supervisory system taking account of countries' specificities should be established to optimize the advantages that a given country can gain from the S&D provisions and from the multilateral trading system as a whole.

108. Switzerland supports the "*Cotton Initiative*" launched by West African countries in 2003, and has proposed three-fold action: first, the relevant organizations should work in favour of reducing the short-term problems of these countries by modernizing and restructuring the cotton sector, including in areas such as loans to small producers, quality management and transport infrastructure; second, WTO Members should give tax and quota-free access for cotton and cotton products from the poorest countries and substantially reduce levels of distorting domestic support in cotton in particular and eliminate all types of export subsidy as an integral part of the negotiations on agriculture; and third, if the negotiations on agriculture do not produce the desired result on cotton, specially adapted measures should be found.

109. Switzerland intends to participate actively in the *definition of modalities*, in negotiations on trade facilitation, and in all the fields of negotiation during the next negotiating phase of the Doha Round. The WTO is facing major challenges: the globalization of inter- and intra-enterprise relationships and the very rapid growth of markets demands corresponding changes in the rules of international trade. This is why Switzerland believes that the results of negotiations should not just be circumscribed to figures, but should also lay down rules that will be properly applied by all parties involved in international trade. Switzerland also wants more transparency during the negotiations themselves. All the different shades of opinion represented among the 148 WTO Members should be

heard so that, at the end of the day, each and every Member can declare "ownership" of the results which will have to be balanced. This also means that efforts will have to be redoubled to arrive at better dialogue with parliaments and between parliaments, with NGOs and between NGOs. Significant progress at this level is indispensable for current trade policy objectives to be realized as a whole.

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REPORT BY LIECHTENSTEIN

I. INTRODUCTION

1. Since the first WTO trade policy review of Switzerland–Liechtenstein in the year 2000 the development of Liechtenstein can be characterized by a consolidation process. In the years 1995-2000 Liechtenstein joined the European Economic Area (EEA)[37], the World Trade Organization (WTO) and the Agreement on Government Procurement of the WTO (GPA). These steps led to far-reaching legal and organisational adjustments in Liechtenstein. The years after 2000 have been a period of completion and fine tuning of these new adjustments.

2. Liechtenstein is highly dependent on external relations. The external economic relations are tremendous: virtually all raw materials and input parts and products have to be bought abroad; a significant part of the value added in the industrial and the services sector goes back to customers abroad; Liechtenstein employs almost as many cross border workers as resident persons (the relation is 0.9:1) and also higher education is gained mainly abroad. Thus, Liechtenstein's economic operators have every interest in access to liberalized markets. At the same time the Government has to find a balance between liberalising further Liechtenstein's own market and taking care of Liechtenstein's specific situation due to its limited territory, its limited human and natural resources and the extremely high percentage (66 per cent) of non-Liechtenstein citizens in the workforce.

II. TRADE AND ECONOMIC POLICY ENVIRONMENT

3. Due to international standards and especially the standards of the EEA, Liechtenstein started in the second half of the nineties to liberalize the postal services, telecommunications services and transport services. In the years 2000-04 this liberalization process has continued and structures have been adapted and optimized. In addition, first liberalization steps towards privatization of the electricity and gas sectors have been approved by the Parliament.

4. Great efforts have been put into the creation of new and the improvement of existing laws in the context of financial services in order to comply with international standards. A special emphasis has been given to supervision of financial services (see below).

(1) ECONOMIC GROWTH

5. In the years 2000-04 growth figures of the previous years could not be repeated. The economic indicators reflect a period of stagnation. Since 2003 the Liechtenstein economy started to recover. The GDP increased from 4,002 million Swiss francs (1999) to 4,195 million Swiss francs in 2000 and to 4,205 million Swiss francs in 2001. From 2000 to 2001 there was a sharp decrease of the GNP (-8%) and of the national income (-9,6 per cent). Total employment in Liechtenstein increased from 26,797 (2000) to 29,055 (2003) employees. Industrial exports[38] decreased from 4622 million Swiss francs in the year 2000 to 4422 million Swiss francs in 2001 and to 4294 million Swiss francs in the year 2002 but rose again by 8.2 per cent to 4,646 million Swiss francs in the year 2003. Exports to Switzerland remained at around 12 per cent of the overall exports. In the year 2003, exports to EEA-Members increased by more than 10 per cent up to 1816 million Swiss francs (43 per cent of the overall exports). Exports to other countries (44 per cent of all exports) also increased by 9 per cent. By individual countries the main destinations were the US (641,9 million Swiss francs), Germany (596.5 million Swiss francs) and Switzerland (595,2 million Swiss francs). Within the

[37] See explanations under III (2).
[38] Only including firms which are member of the Liechtenstein Chamber of Commerce and Industry.

Asian countries, Taiwan ranks before Hong Kong and Japan as export destinations. In 2003, the Liechtenstein export industry has not increased employment in Liechtenstein but has opened 18 branches abroad. The number of employees in 195 branches of the Liechtenstein exporting industry outside of Liechtenstein went up from 23,611 to 26,873.

6. The total balance sheet of the 16 banks in Liechtenstein decreased from 36,964 million Swiss francs in the year 2000 to 34,788 million Swiss francs in the year 2001 and to 32,665 million Swiss francs in the year 2002. In the year 2003, it increased again up to 34,908 million Swiss francs. The net profit of the banks and client assets under management have shown a similar pattern during these years.

7. Liechtenstein has the same inflation rate as Switzerland (2000: 1.6 per cent, 2001: 1.0 per cent, 2002: 0.6 per cent, 2003: 0.6 per cent). Interest rates remained stable with some slight decreases. There are no figures available reflecting private consumption or investment. The unemployment rate in Liechtenstein is traditionally very low; the maximum rate so far has been 2.4 per cent (2004).

8. The development of the Liechtenstein national budget in the period 2000-03 was determined by several factors, including the performance on the stock exchanges, which had an effect on the capital reserves. The current expenses surged from 596 million Swiss francs in 2000 to 664 million Swiss francs in the year 2003. Tax income steadily increased until 2001, but declined in the subsequent two years. The overall state income decreased from 829 million Swiss francs in the year 2000 to 794 million Swiss francs in the year 2003. The current expenses have been affected by the exchange losses on reserve assets (managed by external asset managers) in these years. In the year 2002 Liechtenstein had the first negative national budget (-47 million Swiss francs and -57 million Swiss francs for the current budget and overall budget respectively) since many years. The "own capital" steadily lies at 1.7 billion Swiss francs. In 2003 and 2004, the Government has proposed several measures to cut expenditure and has also changed the (management) criteria for its investment policy.

(2) THE ECONOMIC SECTORS

9. The highly industrialized economy of Liechtenstein is characterized by a broad diversification of sectors, businesses and products. The average value added is very high, based on research and development, qualified expertise, a wide range of high-tech and niche products, strong export orientation, and a highly developed financial services sector.

10. The employment figures in Liechtenstein are extraordinarily high. With a population of 34,000, there are 29,000 jobs. This considerable level of employment can be explained by the fact that the number of cross-border commuters to Liechtenstein is many times higher than the number of cross-border commuters from Liechtenstein. About 13,000 individuals commute daily from the region (Austria, Switzerland and Germany) to their workplace in Liechtenstein. This is about 45 per cent of the total work force. As of 31 December 2003, jobs were partitioned as follows: 53.7 per cent in commerce and services, 45 per cent in industry and manufacturing, and 1.3 per cent in agriculture and forestry. By international standards, the very low proportion of agriculture and forestry is striking, as is the relatively high proportion of the manufacturing sector. The services sector is considerably smaller than in other European countries.

11. About 40 per cent of the GDP is the result of value added in industrial production and manufacturing, 30 per cent in the financial services sector, 25 per cent in general services, and the remainder in household, agriculture and forestry. The industry and manufacturing sector counts for

559 businesses. More than 70 per cent of these are small businesses (1 to 9 employees) while nine companies have more than 250 employees. In 2002, the commercial economy encompassed 3,015 businesses. The employees of these businesses work in 125 professions, 95 of which are apprenticeship professions.

12. Liechtenstein has evolved in the last fifty years from an almost purely agricultural State into one of the most highly industrialized countries in the world. The most important branches of the industrial sector are mechanical engineering, plant construction, manufacturing of precision instruments, dental technology, electronic control devices, vacuum, heating and lighting technology, dentistry and pharmaceutical products and food-processing industry. The per capita value of exports is about five to eight times higher than the corresponding value for Germany, Austria or Switzerland. With 292 million Swiss francs, the expenditures in 2003 for research and development of industrial companies belonging to the Chamber of Commerce and Industry amounted to over 8,000 Swiss francs per inhabitant.

13. Financial services are an important economic sector in Liechtenstein, but not the largest. Seventeen per cent of persons employed in Liechtenstein work in the financial sector. The services offered include in particular asset management, international asset structuring, investment funds as well as insurance and re-insurance business. Sixteen banks, 385 asset managers and trust companies, 23 Liechtenstein insurance companies, 185 insurance companies from abroad engaging in free movement of services (within the EEA) and 17 fund management companies with 190 investment funds operate in Liechtenstein. Liechtenstein banks manage assets in the amount of 104 billion Swiss francs as of end 2003. The assets in Liechtenstein investment funds currently amount to 14 billion Swiss francs. The close treaty relationship with Switzerland, the introduction of the Swiss franc as legal currency and the passing of the 1926 Act on Persons and Companies, that allowed for a broad selection of company forms, as well as an investor friendly tax system, are the foundation on which Liechtenstein's financial center is built. The last 15 years have been a particular dynamic period for the Liechtenstein financial center. The accession to the European Economic Area in 1995 acted as a catalyst for a series of fundamental changes and facilitated access to the markets of other countries.

14. The Government is the primary authority for licensing all banking, investment, and insurance activities. In order to further strengthen the quality of the financial center, the Parliament has passed in June 2004 a bill establishing an independent integrated financial supervisory authority, consolidating the current functions of the agencies involved in financial sector supervision and regulation. As an EEA member, Liechtenstein is obliged to implement relevant EU legislation. Accordingly, banking, insurance, securities and accounting legislation is based on the relevant EU Directives. Because of the close monetary links with Switzerland, financial institutions are also required to meet the accounting guidelines of the Swiss regulatory authority. Banks, insurance firms or funds companies with no physical presence are not permitted.

15. Liechtenstein has a vital interest in the worldwide enforcement of internationally recognized standards to prevent abuse of the financial markets. Liechtenstein's foreign policy therefore pays great attention to the development and international enforcement of uniform rules to combat money laundering and the financing of terrorism. At the national level, legislative, administrative and other practical measures have been taken in the last years to achieve this goal, and the relevant standards in Liechtenstein have been acknowledged by international bodies such as the International Monetary Fund (IMF). In 2002, Liechtenstein underwent an Offshore Financial Center Assessment by the IMF. In their report of September 2003, the IMF experts attested Liechtenstein's preventive measures against money laundering and financing of terrorism a "*high level of compliance with international standards",* including, a high degree of implementation of the FATF (Financial Action Task Force)

recommendations on combating money laundering as well as the 8 special recommendations of the FATF on combating the financing of terrorism.

16. The primary sector employs 1.3 per cent of the total workforce. The number of employees in the primary sector remained stable during the past four years. Two thirds of the gross agricultural return is produced by the dairy industry.

17. Liechtenstein's economic life has benefited from social harmony for many years. The relationship between employers and employees is a peaceful and co-operative one. The country has a fully-fledged social welfare system.

(3) STATE ACTIVITIES

18. The Government of Liechtenstein does not provide any export subsidies, support of research, structural policy nor any subsidies to companies. Furthermore, the Government has no possibility to influence an exchange rate increase of the Swiss franc. The main features of the playing field set by the Government's economic policy are trade laws, sound (mainly positive) budgets, low taxes, stability and reliability of the policy, the creation of high quality educational systems, low administrative burden and a slim and customer oriented public administration.

19. In order to maintain and expand the favourable economic conditions in Liechtenstein the Government participated in the foundation of a Competence Center for Small and Medium-Sized Enterprises (SME) under the direction of the Liechtenstein University of Applied Science. This Competence Center supports SME in their start-up phase. The Center advises young professionals and companies in the growth phase on business planning and management, arranges contacts with financial institutions, investors or potential business partners.

20. Due to the country's small territory (160 square kilometres) and in view of the relatively high proportion of non Liechtenstein citizens of the total of the resident and of the working population (34,5 per cent and 65,3 per cent respectively) Liechtenstein regulates new investments (green field investments) and immigration. By regulating foreign direct investments (also for non-resident Liechtenstein citizens) the Government respects the limited area with its rural character of Liechtenstein and preserves access to real estate for the resident population. Compared to the last Trade Policy Review Switzerland-Liechtenstein the portion of non Liechtenstein citizens of the resident and of the working population has even increased. Therefore, the Government does not see any leeway to ease restrictions concerning immigration and employment. In view of this specific situation, Liechtenstein has, even in the EEA, special rules for the free movement of persons.

(4) PROSPECTS

21. The economic prospects for the near future are good due to the social, legal and economic stability that Liechtenstein's location provides. There are, however, constraints for further growth, namely the very low supply of and the high prices for land and property as well as the dried-out labour market. An external factor that might have a slowing down effect on the economic growth is the revaluation of the Swiss franc.

III. TRADE POLICY DEVELOPMENTS AND FUTURE POLICY DIRECTIONS

22. The framework of the trade environment of Liechtenstein is outlined by the Customs Union Treaty with Switzerland, Liechtenstein's membership in the European Free Trade Association (EFTA), the EEA and the WTO. These vessels allow Liechtenstein to participate in the multilateral trading system but at the same time to join as a complementary tool greater economic cooperation in

regional agreements. Trade agreements are important tools for a small and highly export oriented country such as Liechtenstein. These agreements allow Liechtenstein's economic operators to trade on rule-based systems. So far Liechtenstein has not been involved in any WTO or EFTA dispute case.

(1) THE WORLD TRADE ORGANIZATION (WTO)

23. Liechtenstein is fully committed to the multilateral rules-based trading system and will continue to emphasise the importance of universal broad-based trade liberalization. Liechtenstein strongly advocates the Doha Development Agenda and the Doha Work Programme and remains firmly committed to its successful conclusion. The WTO system has to respond with flexibility to the realities and needs of this century's economy and to the increasingly diverse situations of its members. Improved market access means more trade, and more trade is beneficial to all, developed and developing countries alike. It also offers opportunities for growing trade among developing countries. The Doha Round has also to be a development round to help developing countries to profit from these new opportunities. The multilateral trading system is a proven vehicle in promoting economic development and growth and is central to the future prosperity of our nations. In the view of Liechtenstein there exists no alternative to the WTO multilateral trading system. The multilateral system has to be strengthened.

24. Liechtenstein's agricultural sector is not only small in absolute but also in relative terms. It accounts for only one percent of employment. Liechtenstein is a net food importer. Agriculture in Liechtenstein is more than just food production. The Liechtenstein agricultural sector has in the last decades and years gone through tremendous structural changes. This sector has to be looked at from political, social and environmental perspectives. Non-trade concerns have to be duly taken into account when talking of progressive liberalization steps of this sector. WTO has to allow Members to follow different objectives with their agricultural policy than only trade. Liechtenstein of course is ready to look into agricultural reforms.

25. As necessary flanking measures for Liechtenstein, the extension of protection of geographical indications to products other than wine and spirits should absolutely be part of WTO.

26. Despite more than 50 years of tariff negotiations, non-agricultural market access is still an unfinished business. Further progress has to be achieved during this Round, in particular in areas of export interests to developing countries. Liechtenstein supports further substantial reductions in custom duties and their comprehensive binding.

27. Services form an important part of the overall package of the current negotiating Round. Services account for a large part of economic growth, both in industrialized and developing countries. Liechtenstein has handed in a comprehensive offer last year.

28. As the outcome of the negotiations should be beneficial to all, Liechtenstein welcomes that specific concerns of developing countries are addressed in all areas of the negotiations.

(2) THE EUROPEAN ECONOMIC AREA (EEA)

29. The Agreement on the European Economic Area extends the single market of the EU to the three EFTA countries Iceland, Liechtenstein and Norway. This means that the four fundamental freedoms of the internal market of the EU, the free movement of goods, services, capital and

persons[39], apply within the EEA mainly in the same way as in the EU. In addition, the Agreement includes flanking and horizontal policies in order to strengthen the internal market. These horizontal policies include research and development, statistics, education, social policy, the environment, consumer protection, tourism, small- and medium-sized enterprises, culture, information services and audiovisual services. The membership entails the obligation to transpose EU single market legislation into national law and to comply with supervisory law standards and principles applicable to the entire EEA. By 2003, the overall number of adopted legal acts amounted to 4037.

30. Liechtenstein became a Member of the EEA Agreement on 1 May 1995 in order to secure its economic success on a long term basis. This was a radical step for Liechtenstein, requiring concentrated action at the political and administrative levels over an extended period of time, as well as far-reaching legal and organisational adjustments, also in order to preserve the customs union between Liechtenstein and Switzerland. However, the efforts have been worthwhile – the outcome has been largely positive.

31. Clearly, the EU is the most important market for Liechtenstein's economic operators and the EEA with its four freedoms has given them an appropriate legal framework. As a consequence of this agreement, a large part of Liechtenstein's economic legislation is based on EU law. At the end of 2003, Liechtenstein had implemented more than 98 per cent of the relevant internal market rules, which is above the EU average.

32. In the period 2000-04 the most important development for the EEA was its enlargement due to ten new EU Member Countries. An enlargement Agreement for the EEA was negotiated with the EU, its Member Countries and the new EU Members. Basically, the adaptations to the internal market rules negotiated for these accessions within the EU (transitional periods for the free movement of persons, etc.) have been taken over into the EEA Enlargement Agreement. The three EEA-EFTA States, Iceland, Liechtenstein and Norway, have established their own financial mechanism to co-finance projects for the development of disadvantaged regions in the enlarged EU. Since 1 May 2004, the EEA Enlargement Agreement is applied provisionally until all EU Members have ratified, which is expected in autumn 2004.

33. Although it is difficult to foresee, if, in the longer term, the EEA can be kept in its present form, Liechtenstein is interested to keep this or a similar contractual framework for economic relations with the EU. Adaptations might in particular be necessary, should one or the other EFTA State change its integration policy toward the EU.

34. The relationship between Liechtenstein and the EU is not limited to the EEA and in the coming years, the cooperation might widen in scope. In 2004, Liechtenstein has concluded negotiations with the EU on the taxation of saving interests, a treaty that should soon be signed. Exploratory talks are also conducted on an association in the so-called areas of Schengen and Dublin (open borders, visa, asylum, etc.), in parallel to a similar Swiss Association. Such an opening of the borders would further strengthen Liechtenstein's political and economic ties to its eastern neighbour, Austria.

[39] In the EEA Liechtenstein has special rules as far as free movement of persons is concerned, by which nationals of EEA States are still subject to a permit from the Liechtenstein authorities to take up residence in Liechtenstein.

(3) THE EUROPEAN FREE TRADE ASSOCIATION (EFTA)

35. Liechtenstein became a full EFTA member on 1 September 1991. Hitherto, Liechtenstein had been covered by the EFTA Convention through a particular Protocol under which the interests of Liechtenstein were taken care of by Switzerland.

36. In June 2001 EFTA-Ministers signed an updated EFTA-Convention that entered into force on 1 June 2002 in parallel with the bilateral Agreements between Switzerland and the EU. For the first time since the signing of the EFTA Convention in Stockholm in 1960 Member States agreed to substantial changes to the Convention. The conditions for trade in goods have been improved by removing technical barriers to trade, allowing for mutual recognition of certification of industrial products and facilitating trade in certain agricultural products. Substantial new provisions have been introduced on the free movement of persons, investment and services, public procurement and intellectual property rights. The updated Convention creates conditions between the EFTA States that in many respects are similar to those between the EFTA States and the EU, provided by the EEA Agreement and the bilateral Agreements between Switzerland and the EU.

37. EFTA's network of contractual relations is continuously expanded according to its policy of making a dynamic and independent contribution to improving economic conditions across Europe and beyond and of forging strong links with trading partners outside the continent. Due to the EEA-Enlargement in May 2004, eight of the existing 20 free trade agreements have been replaced by the EEA Agreement.

38. Since 2000 the EFTA States have concluded new free-trade agreements with Croatia, Jordan, Macedonia, Mexico, Singapore. An Agreement with Chile has been signed in June 2003. It will enter into force in 2004. With Lebanon an Agreement has been signed in June 2004. They have in addition signed since 2000 declarations of cooperation with Algeria, the Gulf Cooperation Council, Mercosur, Serbia and Montenegro and Ukraine. Free trade negotiations with Tunisia and Egypt are nearly finalised. Negotiations with SACU (Southern African Customs Union) are in progress. A first round of free trade talks with South Korea has taken place in August 2004.

(4) CUSTOMS UNION TREATY/ECONOMIC INTEGRATION WITH SWITZERLAND

39. The close cooperation with Switzerland is reflected in many (more than 50) bilateral treaties, the most important of them being the Customs Treaty and the Currency Treaty. The Customs Treaty, in combination with other agreements pertaining to the movement of persons, made possible the abolition of any border or customs control between the two countries. Of equal practical importance to Liechtenstein's economy is the Currency Treaty which forms the legal basis for using the Swiss franc as the official currency in Liechtenstein.

40. The provisions of the Customs Treaty stipulate that the Swiss laws pertaining to customs as well as other federal legislation necessary for the implementation of the customs-free zone are applicable in Liechtenstein. In addition, trade and customs treaties concluded by Switzerland with third parties (with the exception of the EEA countries) also apply to Liechtenstein on the basis of the Customs Treaty. Switzerland is authorized to represent Liechtenstein in relevant negotiations and to conclude such treaties with effect in Liechtenstein.

41. The treaty facilitated the bilateral cooperation far beyond its original scope of application, in particular in the areas of social welfare (health, social security), education (vocational and professional training), transport and environment.

42. The entry into force of the EFTA Convention on 1 June 2002 (see above) has led to an additional integration step in the relations between Liechtenstein and Switzerland. Substantial new provisions with regard to the relationship between the two countries have been introduced mainly on the free movement of persons and public procurement. The other updates of the EFTA-Convention have brought only marginal improvements to the already existing status quo.

43. Future developments of the existing close links between the two countries will strongly depend on the integration policy both countries will choose towards the EU.