

# CREDIT INSURANCE FOR EXPORTS AND THE GENERAL AGREEMENT ON TARIFFS AND TRADE

*Rafael E. Cañas*\*

*Eric Scharf T.*\*\*

By the end of World War II, increased efforts have been made to limit the enforcement of certain trade barriers which affect international trade, hinder the competition between countries, and prevents the globalization of a free-market system. It is in this light, that endeavors have taken place to avoid export credit subsidies from becoming a competitive element in international transactions.

The General Agreement on Tariffs and Trade<sup>1</sup> [hereinafter GATT], which was opened for subscription as of October 30, 1947, is one of the most important international judicial instruments that regulates and seeks the elimination of export credit subsidies. As will be discussed later, there are cases when export credit insurance could be considered as a credit subsidy for exports which would be prohibited by GATT.

Due to the fact that Costa Rica is one of GATT's signatory countries, and since GATT is recognized as part of the law of our country,<sup>2</sup> it is necessary to study the regulations established in relation to export credit insurance through subsidies. Thus, we should first analyze the types of financing for exports that are generally used, then analyze the reasons for considering some of those financing systems for exports as subsidies, and finally an analysis to determine if credit insurance for exports is prohibited by GATT.

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\* University of Costa Rica (Attorney at Law and Notary Public, Honors, 1994). Degree Exams Jury, Autonomous University of Central America, 1994. Member: Costa Rican Bar Association; Philip C. Jessup Costa Rican International Law Association.

\*\* University of Costa Rica (Attorney at Law and Notary Public, Honors, 1994). Professor Roman Law, University of Costa Rica Law School, 1995 - Member Costa Rican Bar Association; Philip C. Jessup Costa Rican International Law Association.

1. General Agreement on Tariff & Trade, Oct. 30, 1947, 61 Stat. A-11, T.I.A.S. No. 1700, 55 U.N.T.S. 194 [hereinafter GATT].

2. Public treaties, international agreements, and concordats, duly approved by the Legislative Assembly, will have from their promulgation or from the day that they designate, authority superior to the laws. LA CONSTITUCION POLITICA DE COSTA RICA, art. 7.

In the first place, we should indicate that the liberalization of the markets in the past years has caused international transactions to acquire greater relevancy and importance, not only for exporters that carry them out, but also for the countries in which such exports originate. Accordingly, governments have increased the application of policies which tend to increase exports, including the creation of financial systems for such operations.

Some of the most important forms of financing for exports<sup>3</sup> can be cited as follows:

- 1) Grants of credit for exporters, constituted by loans given by the government or by private banks, in favor of foreign importers or national exporters, which permit the final buyer to defer payment of the price of goods or products imported.<sup>4</sup>
- 2) The possibility of acquiring credit insurance for exports, usually guaranteed by governmental insurance agencies, in order to transfer the assumption of risks that may be created by defaults on payment of the export operation's price which may or may not have been financed through credit for exports.
- 3) General governmental assistance which tends to facilitate the development of operations for exporters, and consequently acts as an incentive for these to increase.

In spite of the great importance that these financing systems represent for exports, such mechanisms should not be converted into key elements for the development of competition in the international market. In other words, the effect of financing the credit for exports should be neutral, and such a mechanism should not have an effect on determining the conclusion of an international sale or purchase.<sup>5</sup>

On the other hand, financing exports could be used as subsidies for exports, something which could effect the competition between countries and impede the operation of a free-market system. In fact, to the extent in which governments have increased their support for the financing of credit

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3. See Filip Abraham, *The Effects of Intra-Community Competition of Export you Subsidize to Third Countries: The case of export credits, export insurance and official development assistance*, Office for Official Publications of the European Communities, Lux. 1 (1990).

4. See Andrew M. Moravacsik, *Disciplining Trade Finance: The OECD Export Credit Arrangement*, 43 INT'L ORG. 173, 176 n.1 (1989).

5. "The effect of export credit financing on a sale should be neutral, and such financing should not be used to provide an enticement to conclude a sale." Orit Frenkel & Claude G. B. Fontheim, *Export Credits: An International and Legal Domestic Analysis*, 13 LAW & POL'Y INT'L BUS. 1069, 1085 (1981).

and insurance for exports, it has intensified competition between countries to offer buyers the most attractive incentives at the least possible cost.<sup>6</sup>

The following instances are examples of financing systems which could be considered as subsidies: where credit is given at interest rates much lower than the rates available on the domestic market; or where credit insurance is acquired for exports with premiums inadequate to cover the contingent losses caused by the default of credit conferred to the importers.

In order to avoid the aforementioned situations, GATT, like other international instruments, has regulated the utilization of subsidies for exports. Originally, article XVI of GATT compelled signatory countries to report all of the subsidies they give for the purpose of increasing exports or reducing imports.<sup>7</sup>

During the sessions held in 1954 and 1955, article XVI of GATT was amended to include the following two prohibitions:<sup>8</sup> 1) Signatory countries were prohibited from utilizing subsidies for the exportation of primary product exports when they considerably distorted the international marketing of those products, and 2) Prohibition the utilization of subsidies for non-primary export products if they permitted the export of goods at a lesser price than that established within the exporting country.

As a result, in the 1960s a special commission presented a report which listed practices that should be considered subsidies (under article XVI). In April 1979 the Code of Subsidies [hereinafter the Code] was approved. It consisted of an agreement on the interpretation and application of article XVI of GATT, as well as other provisions.<sup>9</sup> The Code prohibited policies of governments (or special institutions controlled by the State) which insure and guarantee credit for exports that protect against the increase in the costs of products of exportation or exchange risks, thereby, eliminating them as subsidies.<sup>10</sup>

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6. "As governments have turned increasingly to support export credit and insurance/guarantee financing, competition among nations to provide the most attractive inducements or features at the lowest cost to the buyer have intensified." *Id.* at 1070.

7. GATT, *supra* note 1, at art. XVI.

8. *Id.*

9. *Id.*

10. The provision by governments (or special institutions controlled by governments) concerning export credit guarantees or insurance for programs against increases in the costs of exported products or of exchange risk programs, at premium rates, manifestly inadequate to cover the long-term operating costs and losses of the programs. Agreement on Interpretation and Application of Articles VI, XVI and XXIII of the General Agreement on Tariffs and Trade, Apr. 12, 1979. GATT *supra* note 1, at arts. VI, XVI, XXIII.

Credit insurance for exports is mentioned specifically as one of the subsidies for exports prohibited by the Code of Subsidies interpreting GATT. However, this version of the Code is not the most appropriate because some scholars have interpreted this prohibition and have come to the following conclusions:

- 1) The article only prohibits insurance against risk of change or an increase of price in the exported product. It could be interpreted that such prohibition is not applicable to other types of risks.
- 2) Only credit insurance programs are prohibited for exports in which the premium is insufficient. First of all, the distinction between long and short term does not remain clear. Aside from this, based on the foregoing, we can interpret the following:
  - a) It is possible to insure all types of exports if the tariff of the premiums is well calculated and is equivalent to the contingent costs and losses that could be caused by default in payment of the operation.
  - b) Long-term operations are not insurable if the premium is inadequate to cover its contingent costs and losses. However, it may be possible to insure short term operations whose premiums retain those characteristics.
- 3) Only credit programs and credit insurance for exports that are funded by the government of the exporting country or by the institutions controlled by that government are prohibited. We can interpret that to mean that GATT does not prohibit any type of insurance that is acquired from private insurance companies.

In conclusion, and analyzing the case of Costa Rica, GATT, and the respective Code of Subsidies, specifically prohibit the implementation of credit insurance for exports. However, such prohibition is not applicable to the credit insurance for exports offered by the National Insurance Institute for the following reasons: 1) The types of exchange risk currently protected by the credit insurance for exports offered in Costa Rica are not found to be included within the prohibition of the Code of Subsidies, and 2) Such prohibition will not be applicable to the case of the National Insurance Institute; since, according to officials and ex - officials of the institution, the calculation of premiums is carried out through a very complex procedure that assures the proportionality and correspondence between the amount of the premium and the contingent damages and losses that could be suffered by the exporter in case of credit default on the part of the importer.