

can their *forfeiture* be adjudged by the court. But the OICs and their task forces, would be acting beyond their powers of *preserving* sequestered assets, when they interfere and even want to control the management and *operation* of commercial business by private enterprises.

In my appearance as *amicus curiae*, I tried to clarify the Constitution (sic) on the right of the State to recover ill-gotten wealth (Sec. 15, Art. XI). That is not only mentioned in Proclamation No. 3 (the Freedom Constitution), and in Executive Orders Nos. 1 and 2 and Executive Order No. 14 of the President, but it is also recognized in the Transitory Provisions of the new Constitution (Sec. 26, Art. XVIII).

During the plenary sessions of the Constitutional Commission I suggested that the transitory provision on the PCGG should state that judicial *action* be filed within *six months* after the issuance of the sequestration order. Some Commissioners made a distinction between sequestration orders issued *before* the ratification of the Constitution and those that will be issued *after* its ratification on February 2, 1987. I replied that the transitory provisions have reference to the transition from the Freedom Constitution to the new Constitution. The actions and powers of the PCGG do not have material relevance to the ratification of the Constitution. However, my proposal was amended to the effect that sequestration orders issued *before* the ratification of the Constitution (the Government) would still have six months *after* said ratification to file the required civil action. Some sequestration orders have been issued on April or May 1986, and judicial action may still be filed within six months after February 2, 1987. In my opinion that period is too long. Because in our earnest policy to recover ill-gotten wealth as plunder of our national wealth, the function of the PCGG may still be extended by law. We have to restore political normalcy to encourage more investments, both domestic and foreign and continue our program of productivity based on sound agricultural development and promote industrialization and full employment (Sec. 1, Art. XII).

My friends, I would like to say that one of the state policies, which I suggested and was adopted reads:

"Sec. 20. The State recognizes the indispensable role of the private sector, encourages private enterprise, and provides incentives to needed investments." (Art. II)

I have warned my fellow Commissioners against so many monetary burdens and financial obligations on the State, like highest budgetary priority for Education (Art. XIV) with free elementary and secondary public education (Sec. 2(2)) and also to Social Justice (Art. XIII) when the State, may not have sufficient resources to undertake such laudable projects. The private sector not the Government, can increase productivity and create additional sources of wealth.

The provision in the fundamental principles which I suggested and was also approved reads:

"The maintenance of peace and order, the protection of life, liberty and property, and the promotion of the general welfare are essential for the enjoyment by all the people of the blessings of democracy." (Sec. 5, Art. II)

Manuel A. J. Teehankee *

1.0 INTRODUCTION

Countertrade, according to estimates, now accounts for between 20 to 30 percent of world trade and by some projections could account for 50 percent of world trade by the year 2000.¹ OECD studies in the mid-1970s had estimated that 40 percent of developing country trade (North-South trade) was covered by countertrade arrangements and this figure is believed to be higher for the present.² Authorities are in dispute as to the actual figures but most are in agreement that the trend towards the use of countertrade is growing and the National Foreign Trade Council of New York as of 1984 listed 88 countries as requiring countertrade in some form while in 1972, only 15 countries were listed as doing so.³

Various factors have contributed to the resurgence of barter in the modern economy in the form of countertrade and the main reason cited is the hard currency shortage faced by developing countries and the world in general as triggered by the two oil shocks of the 1970s.⁴ In the 1980s, a new factor may serve to promote countertrade and at the same time subject it to more scrutiny, i.e., the rising tide of protectionism in the developed world.⁵ GATT studies predict that the growth of international trade will drop from 9 percent last year to only 2 or 3 percent this year, citing among other reasons, increased "voluntary restraints, quotas and other non-tariff barriers being erected all over the world."⁶ An example of the countertrade effect of protectionism is the U.S. Congress' targeting of textile imports into the United States which has led Thailand, an affected country, to negotiate with the Soviet Union on a *barter* basis for its garment exports.⁷

Countertrade, thus has broad global repercussions, both economic and political. It is the object of this memorandum to look briefly at the various types of countertrade arrangements and to examine them in relation to GATT's legal framework.

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¹McVey, *Countertrade: Commercial Practices, Legal Issues and Policy Dilemmas*, 16 L. & Policy Int'l Business 1, 2 (1984).

²Walsh, *Countertrade: Not Just for East-West Anymore*, 17 J.W. Trade L. 3 (1983).

³Williams, *Not for the Faint or Weary: Legal Aspects of Countertrade*, in Symp. Priv. invest. Abroad 265, 273 (1984).

⁴Zarin, *Countertrade and the Law*, 18 Geo. Wash. J. Int'l Law & Econ. 235, 237-238 (1984).

⁵Note, *Countertrade and Export Trading Companies: Has the United States Joined the Successful Trading Game of Japan and Others?*, 11 Syr. J. Int'l L. & Com. 417, 421 (1984).

⁶Wall Street Journal, Nov. 18, 1985, at 30, col. 1

⁷*Id.*

2.0 COUNTERTRADE: WHAT IS IT?

Countertrade has no standard significance and refers collectively to various methods of "linking" imports with exports.⁸ A 1981 OECD publication attempted to define countertrade as —

... an international operation where the seller is required to accept, in partial or total settlement of his deliveries, a supply of products coming from the purchasing country; the contractual link between the two agreements is not necessarily directly related to the export deal.⁹

Governmental policies and programs as well as commercial and financial considerations result in countertrade arrangements peculiar to the circumstances.¹⁰ Authors have come up with as much as eight types of transactions but for our purpose we shall refer only to the four most basic practices of countertrade.¹¹

BARTER AGREEMENTS

Barter involves the direct exchange of products without the use of money and is the oldest and simplest form of countertrade. This represents a small percentage of barter transactions due to the risks involved in accepting goods as payment.¹² However, barter transactions are increasing in Latin America and South East Asia due to the "credit squeeze" and can serve special situations.¹³ A famous case is Pepsi Co.'s acceptance of Stolichnaya vodka as payment for its exports of Pepsi Cola Syrup to the Soviet Union.¹⁴ An advanced form of barter is the bilateral clearing agreements entered into by sovereign nations for trade of their respective goods over a period of time.¹⁵ Barter has also been resorted to as a means of price undercutting by acceptance of overpriced goods in return, as in the case of the trade of crude oil below the official OPEC prices.¹⁶

SWITCH TRADING

This type of countertrade allows countries with surplus receivables of bartered goods (resulting for e.g. from bilateral clearing agreements) which it does not want, to transfer all or part of the goods to a third party usually through a

⁸Schmitthoff, *Countertrade*, J. Business L. 115 (March 1985).

⁹Note, *supra* note 5, at 420.

¹⁰Walsh, *supra* note 2, at 5.

¹¹See generally McVey, *supra* note 1.

¹²Grabow, *Negotiating and Drafting Contracts in International Barter and Countertrade Transactions*, 9 N.C.J. Int'l L. & Com. Reg. 255, 259 (1984).

¹³McVey, *supra* note 1, at 17.

¹⁴Weigand, *International Trade Without Money*, 55 Harv. Business Rev. 28, 29 (1977).

¹⁵*Id.*

¹⁶McVey, *supra* note 1, at 6 n. 14 and 17; Weigand, *supra* note 14, at 42.

"switch trader," and thereby secure hard currency or some other goods that it has more use for.¹⁷ The goods will have to be sold at a discount which can reach up to 30 percent plus a commission for the switch trader.¹⁸ "Switches" can cause problems to the seller of the switched goods when the goods, in effect, end up being dumped into its regular markets.¹⁹ An example cited is Brazilian coffee, exported to Eastern Europe, a non-traditional market, but which ends up in the international market at prices, not normally possible under the International Coffee Agreement.²⁰ A variation of the switch transaction is the "swap" agreement whereby exactly the same commodities are exchanged in order to save on transport costs.²¹

COUNTERPURCHASE

In this type of transaction, money is exchanged but the seller undertakes to make reciprocal purchases of generally non-resultant products over a period of time.²² Counterpurchase is in prevalent use among developing countries and non-market economies (NMEs) and accounts for the bulk of all countertrade transactions.²³ Indonesia is one country that requires foreign firms selling to its government to reciprocally purchase equal amounts of Indonesian goods.²⁴ There is however also the phenomenon wherein the seller rather than the buyer actively offers to counterpurchase as a method of boosting exports to the buying country and this has been referred to by some as "progressive" or "reverse" countertrade.²⁵

In any case, counterpurchased goods may also end up being switchtraded should the holder thereof be unable to market it himself.

COMPENSATION/BUY-BACK ARRANGEMENTS

Also known as import compensation, industrial cooperation or develop-for-import agreements, the supplier of goods (usually capital equipment or even an entire turn-key plant) agrees to be repaid in resultant output.²⁶ Armand Ham-

¹⁷Weigand, *supra* note 14, at 30.

¹⁸McVey, *supra* note 1, at 20.

¹⁹Weigand, *supra* note 14, at 30.

²⁰McVey, *supra* note 1, at 20; Weigand, *supra* note 14, at 34.

²¹c. Swap: Swap transactions involve the exchange of fungible goods, usually commodities, between four parties to reduce transportation costs. For example, if an American company has a contract to supply a certain chemical to a French company, and a German company has contracted to supply the same chemical to a Mexican company, under the swap, the American company would supply the Mexican company while the German company would supply the French company." Grabow, *supra* note 12, at 257 n. 8.

²²Grabow, *supra* note 12, at 257-258.

²³Walsh, *supra* note 2, at 3.

²⁴McVey, *supra* note 1, at 10 and 13.

²⁵*Id.*, at 22-23.

²⁶Note, *supra* note 5, at 418 n. 9.

mer's \$20 billion countertrade deal with the Soviet Union is an oft-cited example. Occidental Petroleum which supplied equipment for and assisted in the construction of ammonia plants in the Soviet Union undertook to purchase and market the ammonia produced by said plants.²⁷ Compensation or buy-back arrangements vary in complexity and involve substantial sums of money and are long-term in nature.²⁸ Developed countries or multinational corporations derive an advantage in this scheme by assuring to themselves a stable supply of produce or raw materials they require.²⁹

For illustrative purposes, a table of various government programs, related to countertrade, is annexed to this memorandum.

3.0 COUNTERTRADE AND THE GATT LEGAL FRAMEWORK

Free trade theory is one of the key concepts underlying GATT and this is in line with its objective of "de-politicizing" international trade. Some observers "view countertrade as a coercive, anticompetitive practice that serves as an impediment to free and open trade."³⁰ Arthur Dunkel, Director General of GATT, has been quoted as expressing concern "for the continued viability of the GATT as bilateral trading arrangements, including countertrade proliferate,"³¹ and as saying that such "would lead to a politicization of world trade."³² However, as an author has pointed out, a distinction must be made on the underlying reasons for the countertrade:

It should be noted at the outset that countertrade arrangements in themselves are acceptable under the trade rules of the GATT. Whether an agreement is acceptable or not depends not on the arrangement but rather on the motivation. Countertrade arrangements which are undertaken for non-economic reasons, in response to governmental policies and programs, are the countertrade arrangements which create problems for a liberal, multi-lateral trading system.³³

The United States government, for one, has expressed a dual policy towards countertrade — opposing countertrade "if it is government mandated" and "ac-

²⁷McVey, *supra* note 1, at 15-16; Weigand, *supra* note 14, at 34; *see also*, U.S. Int'l Trade Comm'n, Pub. No. 10006, *Anhydrous Ammonia From The U.S.S.R., Report to the President on Investigation No. TA-406-5*, Under Section 406 of the Trade Act of 1974, A-14, 69 (Oct. 1979) (the official report without attachments is also published in 44 Fed. Reg. 61,269 (1979)), U.S. Int'l Trade Comm'n, Pub. No. 1051, *Anhydrous Ammonia From The U.S.S.R., Report To The President on Investigation No. TA-406-6*, Under Section 406 of the Trade Act of 1974, A-21, 103 (Apr. 1980) (the official report without attachments is also published in 45 Fed. Reg. 27,570 (1980)).

²⁸Note, *supra* note 5, at 418 n. 9; *See generally* McVey, *supra* note 1.

²⁹McVey, *supra* note 1, at 22-24.

³⁰McVey, *id.*, at 3 and 57.

³¹Walsh, *supra* note 2, at 10.

³²*Id.*

³³*Id.*, at 9-10.

ceptable" if voluntary and reflective of market forces.³⁴ As another commentator has explained:

Government-mandated countertrade arrangements arguably violate the spirit, if not the letter, of the GATT. The GATT was intended to eliminate or minimize governmental interference with international trade flows in order to maximize the benefits derived from the tariff concessions. Government-mandated countertrade constitutes direct interference with the free flow of goods and can cause trade-distorting effects and imbalances. The coercive element of countertrade restrains free international trade flows and results in the displacement of traditional suppliers of goods by other suppliers who are willing to assume a countertrade obligation, even though their products may be less competitive. Government-mandated countertrade transactions, therefore, tend to defeat the primary goal of the GATT.³⁵

THE MFN CLAUSE

GATT Article I imposes upon signatory countries the unconditional Most Favored Nation (MFN) obligation whereby the import and export of goods from and to other signatories are to be accorded nondiscriminatory treatment. The Article provides that "any advantage, favor, privilege or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other contracting parties." This requirement "covers customs duties and charges of any kind" as well as the method of levying such charges and all import-export "rules and formalities."

Given that countertrade requirements are usually *de jure* or *de facto* imposed by the state,³⁶ there is conceivably a violation of MFN if a state does not impose identical countertrade requirements when dealing with exports from all other signatories.

DUMPING AND QUOTAS

Article XI(1) of GATT prohibits the use of quantitative restrictions "or other measures" and it has been argued that countertrade requirements constitute *de facto* quotas or restrictions insofar as they limit imports to the amount of required exports.³⁷ On the other hand, there seems to be little practical value to this as the quantities to be traded are subject of independent negotiations, as in any contract, and the prospective seller would raise the issue at the risk of losing the deal with an NME or LDC government.

Article VI and the MTN "Dumping Code" are quite relevant as dumping, is a natural consequence when companies are under pressure to unload large quantities of unwanted countertraded goods — "often at below the world market price

³⁴Int'l Trade Rep. U.S. Import Weekly (BNA) 58 (Oct. 12, 1983); *see also* related article, 8 Int'l Trade Rep. U.S. Import Weekly (BNA) 893 (Sept. 14, 1983).

³⁵Zarin, *supra* note 4, at 242-243.

³⁶Liebman, *Comment: GATT and Countertrade Requirements*, 18 J.W. Trade L. 232, 252-253 (1984).

³⁷*Id.*, at 254; Zarin, *supra* note 4, at 243-244.

or even below the price which the private firm paid for the goods."³⁸ At least one East-West countertrade transaction has resulted in a preliminary finding of dumping by a local authority.³⁹

SUBSIDIES AND STATE TRADING

Article XVI considers a subsidy as "including any form of income or price support, which operates directly or indirectly to increase exports of any product from, or to reduce imports of any product into, its territory." The 1960 Declaration as well as the new MTN Subsidies Code provide illustrative examples of subsidies which cover a wide range of government incentives such as currency retention schemes and preferential credit terms.

Countertrade has consistently been treated as an alternative method of promoting and financing exports.⁴⁰ As stated in two articles:

The basic unit of any countertrade transaction is the countertrade credit. Governments control these credits either directly or indirectly, through licenses for foreign exchange or other essentials to trade. Countertrade credits can be applied to hard currency or other requirements for imports *that would otherwise not be available from the government*. Governments grant credits *only for certain exports*, and countertrade obligations refer to a specific list of products to which countertrade credit is applied. (emphasis supplied)⁴¹

... countertrade *transfers the cost of marketing a nation's surplus or undesirable products to the private firm*. This transfer provides a valuable benefit to the nation which, some economists will argue, constitutes subsidization of that nation's products by the private firm in the world markets, and creates additional economic distortions and inefficiencies. (emphasis supplied)⁴²

Thus, countertrade is arguably a subsidy or has the effect of one.

Under the GATT and the "second track" of the MTN Subsidies Code, the issue would be whether countertrade in primary products would have the effect of displacing exports of another signatory state.⁴³

The United States acknowledged the possible violation of the above provisions of the Subsidies Code by securing waivers from the principal dairy suppliers

³⁸ McVey, *supra* note 1, at 36.

³⁹ *Id.*, at 40 (USITC preliminary affirmative determination in anti-dumping action resulting from a countertrade agreement with Hungary for the importation of truck-trailer axes. The case was settled before a final determination.)

⁴⁰ See generally McVey, *Countertrade and Barter: Alternative Trade Financing by Third World Nations*, 6 Int'l Trade L. J. 197 (1980-1981).

⁴¹ Williams, *supra* note 3, at 274.

⁴² McVey, *supra* note 1, at 57.

⁴³ GATT Art. XVI: 3; Subsidies Code, Article 10:1.

of Jamaica who would be displaced by implementation of the U.S.-Jamaica barter agreement.⁴⁴

Article XVII which regulates state trading enterprises, imposes a duty of "non-discriminatory treatment," and requires purchases to be made solely on "commercial considerations."⁴⁵ However, as Article XVII expressly allows "tied loans" to be treated as a "commercial consideration." Countertrade, being in essence, a mode of financing transactions for countries short on hard currency, can thus be justified by state enterprises under this provision.⁴⁶ GATT is generally made inapplicable to offset or similar arrangements in government purchases.⁴⁷ However as countertrade, which is closely tied to state trading practices, increases in importance the obligations of governments under Article XVII may come under stricter scrutiny.

DEVELOPING COUNTRIES

Article XVIII and numerous other qualifications in the GATT as well as the MTN Codes, in effect exempt developing countries from the strictures of the MFN clause and other GATT obligations.⁴⁸ Aside from the traditional countertrade practices of NME countries, developing country trade has accounted much for the rapid growth of countertrade. Those in favor of countertrade point out

⁴⁴ See Note, *Bauxite for Butter: The U.S. - Jamaican Agreement and the Future of Barter in U.S. Trade Policy*, 16 L. & Policy Int'l Business 239, 253-254, 254 n. 105 (1984).

⁴⁵ For a more extensive discussion see, Ianni, *The International Treatment of State Trading*, 16 J.W. Trade L. 480 (1982).

⁴⁶ See Liebman, *supra* note 36, at 256-258.

⁴⁷ GATT Art. XVII: 2; see J. Jackson, *World Trade and the Law of GATT* 290-293 (1969); see also new MTN Code an Government Procurement Art. V: 14 (h) and interpretative note thereof which states: (h) entities should normally refrain from awarding contracts on the condition that the supplier provide offset procurement opportunities or similar conditions. In the limited number of cases where such requisites are part of a contract, Parties concerned shall limit the offset to a reasonable proportion within the contract value and shall not favour suppliers from one Party over suppliers from any other Party. Licensing of technology should not normally be used as a condition of award but instances where it is required should be as infrequent as possible and suppliers from one Party shall not be favoured over suppliers from any Party.

Interpretative Notes:

Article V, paragraph 14(h)

Having regard to the general policy considerations of developing countries in relation to government procurement, it is noted that under the provisions of paragraph 14(h) of Article V, developing countries may require incorporation of domestic content, offset procurement, or transfer of technology as criteria for award of contracts. It is noted that suppliers from one Party shall not be favoured over suppliers from any other Party.

⁴⁸ See, e.g., GATT *supra* note 31, Art. XXXVI: 8, para. 8. According to article XXXVI "developed contracting parties do not expect reciprocity for commitments made by them to reduce or remove tariffs and other barriers to trade of less-developed contracting parties." *Id.* This principle is based on the recognition by the contracting parties that there is a need for "positive efforts designed to insure that less-developed contracting parties secure a share in the growth in international trade commensurate with the needs of their economic development." *Id.* para. 3; see also *id.* Art. XXXVIII (stating that contracting parties recognize that less-developed contracting parties need to take protective measures affecting imports); *id.* Art. XVIII, sec. B, para. 9 which provides:

the fact that countertrade serves the objectives of accelerating economic development in the poor nations of the world,³³ consistent with the objectives enunciated by Part IV of GATT. Article XVIII also provides more liberal standards for developing countries invoking the balance of payments exception of Article XII.⁴⁹ To the extent that trade is allowed to continue rather than completely stop, countertrade requirements due to BOP difficulties is justifiable under GATT.⁵⁰ Further, it is often the case that the deals entered into are mutually beneficial and provide the means for long-term projects to be accomplished.

4.0 CONCLUSION

Countertrade appears to be a growing force in international trade and numerous legal and policy issues will have to be confronted. Although countertrade practice, in general, reflects market forces, there is a discernible trend to impose countertrade pursuant to government priorities and objectives that may be inconsistent with free trade or the basic spirit of GATT.

Countertrade and its effects on international trade flows requires more serious study. Suggestions have been made to bring countertrade "under international surveillance."⁵⁴ Until such can be done, Article XXIII of GATT may serve as the vehicle for addressing the issue, should a particular countertrade practice result in nullification or impairment in any manner of a benefit accruing to a signatory state of GATT.⁵²

In order to safeguard its external financial position and balance of payments and to ensure a level of reserves adequate for the implementation of its programme of economic development, a contracting party . . . may . . . control the general level of its imports by restricting the quantity or value of merchandise permitted to be imported; Provided that the import restrictions instituted, maintained or intensified shall not exceed those necessary: (a) to forestall the threat of, or to stop a serious decline in its monetary reserves, or (b) in the case of a contracting party with inadequate monetary reserves, to achieve a reasonable rate of increase in its reserves.

J. Jackson, *supra* note 32, at 25-26." Zarin, *supra* note 4, at 245-246 n. 71.

⁴⁹For example, whereas Art. XII, para. 2 (a) (i) requires an 'imminent threat,' Art. XVIII requires only a 'threat'; whereas Art. XII, para. 2 (a) (ii) requires 'very low monetary reserves,' Art. XVIII requires only 'inadequate monetary reserves'; whereas Art. XII requires that the action to be taken 'safeguard its external financial position and balance of payments,' Art. XVIII permits import restrictions 'to ensure a level of reserves adequate for . . . economic development.'

Zarin, *supra* note 4, at 246 n. 73.

⁵⁰Zarin, *supra* note 4, at 246.

⁵¹McVey, *supra* note 1, at 3.

⁵²Zarin, *supra* note 4, at 244.

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***A brief nine-page article but very to the point in discussing governmental policies and programs that have led to the growth of countertrade.

****The article presumes familiarity with countertrade and analyzes in detail the legal repercussions of countertrade arrangements. It cites numerous material and devotes a seven-page section to GATT issues.