Conditionalities in the Generalized System of Preferences as Instruments of Global Economic Governance

DR. PALLAVI KISHORE

I. Introduction

Developed countries grant non-reciprocal preferential market access to products of developing countries under the Generalized System of Preferences ("GSP"). These grants of preferences are no longer non-reciprocal, however, because developed countries have started to impose conditions for preferential market access. Developed countries place these conditions to achieve their own ends rather than enhance the usefulness of the preferences.

But who decides the conditions to be fulfilled? What role do institutions such as the World Trade Organization (WTO) and its Dispute Settlement Body (DSB) play in deciding the conditions to be fulfilled? It would seem that the WTO being an international organization governs all the countries involved in the GSP schemes. However, the conditionalities in GSP schemes have added another layer of governance—that of the preference-granting country over the preference-receiving country. Thus, conditional GSP schemes serve as an instrument of global governance over the developing countries that receive preferences from developed countries in world trade.

This article will explore the various dimensions of conditionalities in GSP schemes, including their legitimacy, by examining the European Communities (EC)-Tariff Preferences case. It will also look at the stand of the various players involved in the entire process that includes the preference-granting and preference-receiving countries as well as the WTO.

1. Assistant Professor and Assistant Director, Centre for Int'l Trade and Economic Laws, Jindal Global Law School, O.P. Jindal Global University, Sonipat, India.

II. The EC—Tariff Preferences Case

In the EC—Tariff Preferences case, the GSP scheme included five arrangements for granting preferences. The EC granted additional preferences to eleven countries through arrangements meant to combat drug production and trafficking. In 2001, the EC added Pakistan to this list to reward the country for its stand against the Taliban and to improve the EC’s own access to the Pakistani market. India’s textiles exports to the EC declined as a result, leading India to bring a case against the EC at the WTO. This article uses the Appellate Body (AB) Report to analyze conditional GSP schemes as instruments of global economic governance. The analysis is applicable to all GSP schemes containing positive conditionalities.

III. Analysis of Global Economic Governance à travers the EC—Tariff Preferences Case

The EC served as an actor of global governance over the eleven countries by requiring them to fulfill the requirements in the drug arrangements and then over Pakistan by rewarding it for combating terrorism. The GSP and especially its conditionalities are an instrument of global economic governance because they are unilateral schemes prone to modification by the donor countries. Indeed, preference-granting countries may withdraw the GSP benefits altogether if asked to remove the conditionalities. This shows that (potential) beneficiaries are subject to a threat of withdrawal of GSP schemes. In fact, India is the first country to challenge its GSP donor.

India argued the EC could not distinguish between GSP beneficiaries by virtue of the Most-Favored Nation clause, while the EC argued differential treatment of beneficiaries was possible if based on objective criteria such as the needs of developing countries, quoting paragraph 3(c) of the Enabling Clause in support. This is an example of the donor country’s governance over the beneficiaries and the Enabling Clause’s governance over

---

5. This article will examine the impact of the Appellate Body Report on negative conditionalities later.
6. Article I:1 of the General Agreement on Tariffs and Trade reads: "With respect to customs duties and charges of any kind imposed on or in connection with importation or exportation or imposed on the international transfer of payments for imports or exports, and with respect to the method of levying such duties and charges, and with respect to all rules and formalities in connection with importation and exportation, and with respect to all matters referred to in paragraphs 2 and 4 of Article III, any advantage, favour, 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." General Agreement on Tariffs and Trade art. I:1, Oct. 30, 1947 61 Stat. A-11, 55 U.N.T.S. 194 [hereinafter GATT].
7. This paragraph reads as follows: "Any differential and more favourable treatment provided under this clause: (c) shall in the case of such treatment accorded by developed contracting parties to developing countries be designed and, if necessary, modified, to respond positively to the development, financial and trade needs of developing countries." Differential and More Favourable Treatment Reciprocity and Fuller Partici-
the donor countries' GSP schemes. The Clause's interpretation is governed by the WTO DSB, which is in turn governed by the GSP Resolution of the U.N. Conference on Trade and Development (UNCTAD). This became explicit when the Panel referred to this resolution while interpreting the Enabling Clause.

The AB found that GSP schemes must fulfill the non-discrimination requirement stated in footnote 3 of the Enabling Clause. Additionally, the AB found that paragraph 3(c) allows GSP donors to differentiate among beneficiaries based on their needs, but limited the GSP donors' discretion to impose arbitrary conditions by stating that they must treat similarly situated beneficiaries alike. Thus, the AB governs donor countries' GSP schemes by means of ensuring their conformity with the Enabling Clause and in so doing, the AB authorizes the donor countries to govern beneficiaries by differentiating between them by means of conditionalities.

The AB stated that differentiation between beneficiaries must be based on objective criteria stated in the WTO Agreement or international instruments, thus increasing the possibility for GSP donors to add conditionalities including non-economic ones. Thus, international instruments used as conditionalities representing the subjective values of donors are also instruments of governance in their hands to govern the beneficiaries. Also, the AB has made these international instruments govern dispute settlement at the WTO because international instruments can be taken into account in WTO dispute settlement proceedings. However, the criteria the AB laid down to evaluate conditionalities in GSP schemes are still unclear because it did not clarify how its criteria are equivalent to the needs of a developing country, as mentioned in paragraph 3(c) of the Enabling Clause.

After the decision allowing differentiation, India expressed its "fear of a return to the era of special preferences that had prevailed before the GSP had been installed in the trading system." Preferences existed before the GSP in the form of former colonies granting preferential market access to their erstwhile colonial powers. As opposed to the GSP which was generalized, these reverse preferences were selective and discriminatory towards developing countries. The new system of governance of beneficiaries by GSP donors places the generalized GSP schemes developed to remedy this discrimination at risk.

The Decision on Implementation-related Issues and Concerns adopted at Doha states that preferences granted to developing countries should be non-discriminatory, meaning that they are not required to be non-discriminatory. This is contrary to the rule laid down

---

8. This footnote reads: "As described in the Decision of the CONTRACTING PARTIES of 25 June 1971, relating to the establishment of generalized, non-reciprocal and non-discriminatory preferences beneficial to the developing countries" (BISD 185/24). Enabling Clause, supra note 7.


10. Id. ¶ 163.

11. WTO Dispute Settlement Body, Minutes of Meeting, WT/DSB/M/194, ¶ 32 (July 20, 2005).


by the AB. But the Ministerial Conference, which interprets WTO law,\textsuperscript{14} would prevail in a future case because DSB reports are only binding on the parties to a dispute whereas Ministerial Conference interpretations are binding on all WTO members.\textsuperscript{15}

The EC, knowing that its GSP scheme was applicable only to twelve members, asked for a waiver from the WTO.\textsuperscript{16} Since the waiver was not granted, the AB held that the scheme was incompatible with the Enabling Clause. Thus, not only the DSB but other organs of the WTO responsible for granting waivers also govern GSP donors.

Discrimination by GSP donors between developing countries in the form of recipient and non-recipient countries is an example of discriminatory governance. In reality, even uniform application of conditional GSP schemes may result in discrimination because some beneficiaries cannot fulfill the conditions, depriving them of additional preferences.\textsuperscript{17} If these potential beneficiaries could fulfill the conditions, they would not need tariff preferences to encourage their development in the first place.

Furthermore, developing countries face problems apart from drug issues such as lack of healthcare and education facilities. The question then is whether developed countries have absolute discretion to choose the problems for which they grant preferences. It may amount to discriminatory governance if the EC prioritizes drug problems over others, thus discriminating amongst potential beneficiaries with different needs.

Preferential market access eradicates the drug problem in the beneficiary country and reduced market access increases the problem in the non-beneficiary country. But the Enabling Clause does not aim at such a transfer of problems from one country to another. Thus, developing countries such as India that lost market access were actually paying for the countries such as Pakistan that gained market access.\textsuperscript{18} Moreover, in such a case, the recipients of preferences are actors of governance over the non-recipients. India, by filing a case at the WTO, showed its concern for the other non-recipient developing countries, thus being an actor of governance over them.

This case also demonstrated opaque governance, another type of global governance possible. The EC's drug arrangements failed the test laid down by the AB because they were only available to a closed list of twelve beneficiaries without the possibility of other countries benefiting from the drug arrangements, even if the non-beneficiaries shared the same needs as the twelve beneficiaries. The drug arrangements did not lay down the conditions to exclude beneficiaries. Consequently, the beneficiary countries would continue to benefit from the drug arrangements whether or not the arrangements resolved their drug problems. This would provide no benefit to non-beneficiaries that suffered from a drug problem. Once again, the beneficiaries are governing the non-beneficiaries, this time due to lack of transparency in the drug arrangements.

\textsuperscript{14} Article IX:2 of the Agreement Establishing the World Trade Organization reads: "The Ministerial Conference and the General Council shall have the exclusive authority to adopt interpretations of this Agreement and of the Multilateral Trade Agreements."


\textsuperscript{17} India raised this point. See WTO Minutes of Meeting of Trade Policy Review of the European Union, WT/TPR/M/72, ¶ 173 (July 12 & 14, 2000).

The AB allowed only non-discriminatory conditions in GSP schemes to protect against arbitrariness but the UNCTAD resolution authorizing GSP did not envision conditionalities. These conditions are proof of GSP donors’ desire to maintain a certain unilateralism in granting preferences and constitute a form of disguised protectionism. Indeed, developed countries may sometimes use conditionalities to promote their own objectives and could misuse the authority to differentiate between beneficiaries with the aim of favoring certain countries. Thus, on the one hand, the AB wants to govern GSP schemes strictly but on the other hand, it allowed a certain amount of freedom to the GSP donors to govern the beneficiaries.

Some authors feel that developing countries should have anticipated the conditionalities that are sometimes necessary to buy political support for GSP schemes in donor countries. This means that developing countries should have anticipated a relationship of governor and governed to further individual political interests of the former by means of conditionalities.

Apart from these examples of global governance, there is also an example of domestic governance. The decline in textiles exports led the Indian Ministries of Textiles and Commerce to file a case with the WTO, without consulting the representatives of the textiles industry. The industry is the actual producer and thus the motor of international trade although, in developing countries such as India, industry is denied a role in global economic governance because it is not consulted. Instead, the industry is subject to domestic governance in such cases because the domestic government alone decides whether a case should be filed with the WTO. Conversely, there are government mechanisms in developed countries such as the U.S. Trade Representative and European Commission to take into account industry concerns. Consequently, these mechanisms are actors of governance over domestic industry and help industry in developed countries participate in global governance.

Another example of global governance by domestic constituencies is global governance by EC citizens. The EC claimed that the drug arrangements were necessary to protect the health of its citizens under article XX(b) of the GATT, but the argument did not find favor with the Panel. The drug arrangements gave employment opportunities to citizens of beneficiary countries to end the production of drugs reaching European shores. Thus, conditionalities help European citizens participate in global governance over the citizens and governments of developing countries. The EC is an instrument of govern-


22. This article reads: “Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement of any contracting party of measures: (b) necessary to protect human, animal or plant life or health.” GATT, supra note 6, at art. XX(b).
ance over the GSP beneficiaries with the aim of protecting its own citizens, although the primary aim of GSP benefits is to contribute to the development of beneficiaries.

The Appellate Body's Report pertains to positive conditionalities but it will influence future interpretations of negative conditionalities as well. Paragraph 3(c) of the Enabling Clause says that preferences must constitute positive responses to the needs of developing countries, but the question is how will negative conditionalities constitute positive responses. The Appellate Body's Report could lead to a change in GSP schemes from negative to positive conditionalities and to a decline in the number of reasons that qualify as needs that justify differential treatment of beneficiaries. GSP donors may put these conditionalities in bilateral agreements with developing countries because they did not anticipate that the AB would lay down restrictive criteria governing conditionalities. This will be a worse form of governance over the developing countries because they will not have recourse to the WTO DSB. Additionally, developed countries could use a policy of differential preferences to pressure developing countries in multilateral negotiations, which would again be a worse form of governance because there would be no recourse.

After the Appellate Body Report, the EC came up with a new GSP scheme called the GSP Plus. But it also suffered from some defects that revealed the dynamics of the relationship between GSP schemes and global economic governance. The GSP Plus scheme contained three arrangements to benefit from preferences, one of them being the special arrangement to encourage sustainable development and good governance. This arrangement laid down that beneficiaries wanting additional preferences must ratify and implement a list of international conventions that were also mentioned in the previous EC GSP scheme. Thus, the new GSP Plus scheme complied with the AB's criteria, and was not opaque or discriminatory. But, as in the previous case, some developing countries may not be able to fulfill the conditions in the international conventions. In addition, all countries with the same needs may not be able to ratify and implement the conventions. This situation demonstrates how law can be used as an instrument of exclusion. The new EC GSP scheme and the conventions it referred to were legal instruments. According to the European Parliament, the requirement of ratifying and implementing international conventions can create barriers to preferential market access for developing countries. Moreover, countries with different problems must ratify and implement the same conventions. Furthermore, countries' diverse problems are not necessarily reflected in international conventions. More importantly, India stated that similarly situated beneficiaries could not be defined "on the basis of a common commitment to a multitude of international conventions by those beneficiaries," demonstrating the fallibility of the governance exercised by the GSP Plus.

23. Lorand Bartels, European Communities-Conditions for the Granting of Tariff Preferences to Developing Countries and its Implications for Conditionalities in GSP Programmes, in Human Rights and International Trade 484 (2005).
25. Id. at art. 1.2.
27. Minutes of Meeting, supra note 11, ¶ 33.
The EC, by introducing the special arrangement to encourage sustainable development and good governance, that laid down a list of international conventions i.e. required fulfillment of all the criteria mentioned in the previous GSP scheme, tightened the control over developing countries because the previous GSP scheme allowed countries to fulfill the criteria under any of the five arrangements, instead of all the criteria under them.

The GSP Plus scheme allowed the EC to determine the needs of developing countries by means of international conventions that were to be applied in the territory of the beneficiaries. Thus, international conventions served as instruments of global governance by GSP donors over GSP recipients. In addition, the fact that the EC wanted to conform its GSP Plus to international conventions shows the governance exercised by international law over national GSP schemes.

Additionally, the EC imposed non-economic conditions in a GSP scheme that is primarily economic in nature. According to India, the conditionalities also infringed on the sovereign right of each country to decide the conventions it wanted to ratify and implement. Moreover, the special regime to encourage sustainable development and good governance did not benefit countries that had already put into practice, but not ratified, the laws relating to sustainable development and good governance as specified in the international conventions. This is an example of aberrational governance.

After the expiry of Regulation 980/2005, Council Regulation 732/2008 entered into force. Article 1:2 of this regulation, just like its predecessor Regulation 980/2005, establishes a special arrangement for sustainable development and good governance requiring ratification and implementation of a list of international conventions by beneficiaries wanting additional preferences. This means that the present regulation has the same consequences for potential beneficiaries as the previous GSP Plus scheme. Moreover, the current GSP scheme will continue until the end of 2013. There is also a proposal for a revised GSP scheme from Jan. 1, 2014 that reinforces the logic of the current scheme.

IV. Conclusion

While developed nations were free to achieve their development as they wished, including by protectionism, countries developing today face different circumstances. The developed countries can often dictate the terms of economic advancement in developing countries in a way that invokes the old colonialist system.

The conditionalities seek to aid in developing countries' economic advancement by compelling them to respect human rights. But the use of conditionalities is controversial because developed and developing countries often have different stands on the conditionalities attached. Even the stand of the WTO, which also plays a role in furthering human rights (as seen in this case), and that of its members differs. Another shortcoming of conditional GSP schemes is their efficacy. Ratification and implementation of interna-

---

28. Id. ¶ 35.
tional conventions by a country does not necessarily lead to eradication of problems such as child labor since governments may not always function for their people.

This article has shown that conditional GSP schemes create multiple layers of governance that lack utility because they are not coherent. The problem may be resolved by transparent discussions between the key players such as the donors, the recipients, and the non-recipients (i.e. domestic governments and industry) as to how to better achieve the objectives of each actor.