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“A Critical Analysis  
of Conditionalities in the Generalised System of Preferences”

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## **A Critical Analysis of Conditionalities in the Generalised System of Preferences**

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### **Abstract**

This article examines conditionalities in the Generalised System of Preferences (GSP) in light of the European Communities (EC) – Tariff Preferences case at the World Trade Organization (WTO). The article largely undertakes this examination from the point of view of developing countries. However, it also recognises that there may be some merit in the rationale behind the concept of conditionalities. It mainly examines the issue of discrimination in conditionalities since this was the principal question raised in the EC – Tariff Preferences case and makes suggestions regarding the regulation of conditionalities. In doing so, the article follows two trajectories; first, it makes suggestions for the WTO judicial instances and second, it makes suggestions for the GSP donors.

### **Introduction**

The General Agreement on Tariffs and Trade 1947 (GATT) was predicated on the principle of reciprocity<sup>1</sup> and did not recognize any form of differentiation even if it was based on an objective need. This was legalised in the Most-Favoured Nation (MFN) treatment principle in article I.1.<sup>2</sup> Thus, the GATT did not recognise any form of affirmative action. However, developing countries expressed dissatisfaction with the functioning of the GATT and calls to make it development-friendly grew louder. Their argument was that unequal countries could not be treated equally, as required by the MFN treatment principle. Various decisions and declarations favouring developing countries came about but they did not have much impact. The developing countries decided to meet in a separate forum called the United Nations Conference on Trade and Development (UNCTAD). Consequently, the GATT finally accorded a measure of recognition to the demands of developing countries in the form of Part IV of the GATT entitled “Trade and Development” which came into effect on 27 June 1966. This Part encouraged developed countries to open their markets to products of developing countries. It also laid down the principle of non-reciprocity.<sup>3</sup> Of course, this Part was hortatory in nature. This meant that the developing countries were still dissatisfied.

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<sup>1</sup> See recital 3 of GATT which states, “Being desirous of contributing to these objectives by entering into reciprocal and mutually advantageous arrangements...”

<sup>2</sup> This article states, “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.” Despite this article, the GATT contains exceptions in the form of article XXIV which allows customs unions and free trade areas.

<sup>3</sup> See GATT article XXXVI.8 which states that developed countries will reduce or remove obstacles to the trade of developing countries without expectation of reciprocity. The note to article XXXVI.8 in Annex I entitled Notes and Supplementary Provisions states, “the phrase “do not expect reciprocity” means, in accordance with the objectives

This led to more intense work at the UNCTAD culminating in the Generalised System of Preferences (GSP). Its history deserves closer attention since it is the subject of this article. In 1962, the Economic and Social Council of the United Nations (UN) decided to convene a conference on trade and development on the basis of a proposal made by several developing countries.<sup>4</sup> As a consequence, the UNCTAD held its first meeting in 1964 where a resolution on GSP was passed but it did not have binding effect.<sup>5</sup> The GSP is based on the idea of preferential market access. This means that the products of developing countries exported to developed countries would be subject to tariffs lower than those applied to imports from developed countries.<sup>6</sup> This idea emanated from the Argentinian economist Raúl Prebisch, the founding secretary-general of the UNCTAD. Of course, it was not easy to implement and had to face a lot of opposition. Therefore, the developing countries withdrew their recommendation for the establishment of the GSP.<sup>7</sup> The UNCTAD held its second meeting in 1968 in New Delhi where Resolution 21 (II) on “Preferential or free entry of exports of manufactures and semi-manufactures of developing countries to the developed countries” was adopted unanimously.<sup>8</sup> It recognised “the unanimous agreement in favour of the early establishment of a mutually acceptable system of generalized non-reciprocal and non-discriminatory preferences which would be beneficial to the developing countries<sup>9</sup>” and agreed “that the objectives of the generalized non-reciprocal, non-discriminatory system of preferences in favour of the developing countries, including special measures in favour of the least advanced among the developing countries, should be:

- (a) To increase their export earnings;
- (b) To promote their industrialization;
- (c) To accelerate their rates of economic growth[.]<sup>10</sup>”

Thus, the objectives of the GSP were entirely economic in nature, unfettered by the imposition of any conditions.<sup>11</sup>

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set forth in this Article, that the less-developed contracting parties should not be expected, in the course of trade negotiations, to make contributions which are inconsistent with their individual development, financial and trade needs, taking into consideration past trade developments.”

<sup>4</sup> Anthony N. Cole, *Labor Standards and the Generalized System of Preferences: The European Labor Incentives*, 25 Michigan Journal of International Law (Fall 2003), 186.

<sup>5</sup> Anthony N. Cole, *Labor Standards and the Generalized System of Preferences: The European Labor Incentives*, 25 Michigan Journal of International Law (Fall 2003), 187-188.

<sup>6</sup> Norma Breda dos Santos et al., *Generalized System of Preferences in General Agreement on Tariffs and Trade/World Trade Organization: History and Current Issues*, 39 Journal of World Trade, no. 4 (2005), 638.

<sup>7</sup> Anthony N. Cole, *Labor Standards and the Generalized System of Preferences: The European Labor Incentives*, 25 Michigan Journal of International Law (Fall 2003), 190.

<sup>8</sup> Resolution 21 (II) on Preferential or free entry of exports of manufactures and semi-manufactures of developing countries to the developed countries in Annex I A of the Proceedings of the UNCTAD Second Session, New Delhi, 1 February – 29 March 1968, Volume I Report and Annexes, UN, New York, 1968, TD/97, Vol. I, p. 38, footnote 25.

<sup>9</sup> Resolution 21 (II) on Preferential or free entry of exports of manufactures and semi-manufactures of developing countries to the developed countries in Annex I A of the Proceedings of the UNCTAD Second Session, New Delhi, 1 February – 29 March 1968, Volume I Report and Annexes, UN, New York, 1968, TD/97, Vol. I, p. 38, recital 4.

<sup>10</sup> Resolution 21 (II) on Preferential or free entry of exports of manufactures and semi-manufactures of developing countries to the developed countries in Annex I A of the Proceedings of the UNCTAD Second Session, New Delhi, 1 February – 29 March 1968, Volume I Report and Annexes, UN, New York, 1968, TD/97, Vol. I, p. 38, paragraph 1.

<sup>11</sup> In this article, condition and conditionality in the singular and the plural have been used interchangeably.

The GSP could not be established at the international level. Thus, individual developed countries set up their own GSP schemes.<sup>12</sup> This was despite the fact that the benefits of the GSP are contested.<sup>13</sup> Preferential market access, however, violates the MFN treatment principle. In 1971, the Contracting Parties of the GATT granted a waiver for the GSP for a period of ten years.<sup>14</sup> The reason for this temporal limitation was that Raúl Prebisch had advocated the idea of preferences for ten years. The Contracting Parties of the GATT chose to make this waiver permanent in the Tokyo Round. Therefore, they adopted the Enabling Clause on 28 November 1979.<sup>15</sup> There is no temporal limitation in this Clause. Its paragraph 1 states that “[n]otwithstanding the provisions of Article I of the General Agreement, contracting parties may accord differential and more favourable treatment to developing countries [...], without according such treatment to other contracting parties.” The usage of the word “may” indicates that developed countries are not obliged to grant preferences.<sup>16</sup> However, they have to fulfil certain requirements laid down in the Enabling Clause if they decide to grant preferences.<sup>17</sup> European Communities (EC) – Tariff Preferences<sup>18</sup> throws light on the legal status of these requirements.<sup>19</sup> Overall, the Enabling Clause has wider jurisdiction than the 1971 GSP Waiver and includes the notions of non-reciprocity<sup>20</sup> as well as of graduation.<sup>21</sup> It is now part of the GATT 1994<sup>22</sup> and is justiciable.<sup>23</sup>

### **The EC – Tariff Preferences Case**

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<sup>12</sup> Anthony N. Cole, *Labor Standards and the Generalized System of Preferences: The European Labor Incentives*, 25 Michigan Journal of International Law (Fall 2003), 192; James Harrison, *Incentives for Development: The EC’s Generalized System of Preferences, India’s WTO Challenge and Reform*, 42 Common Market Law Review (2005), 1664.

<sup>13</sup> Gene M. Grossman and Alan O. Sykes, *A preference for development: the law and economics of GSP*, 4 World Trade Review, no. 1 (2005), 60-63.

<sup>14</sup> See Waiver, Generalized System of Preferences, Decision of 25 June 1971, BISD18S/24, document L/3545, paragraph a.

<sup>15</sup> The full title of the Enabling Clause is Decision on Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries of 28 November 1979, L/4903.

<sup>16</sup> Also see recital 5 of the Waiver, Generalized System of Preferences, Decision of 25 June 1971, BISD18S/24, document L/3545 which states, “Noting the statement of developed contracting parties that the grant of tariff preferences does not constitute a binding commitment...”

<sup>17</sup> James Harrison, *GSP conditionality and non-discrimination*, 9 International Trade Law & Regulation, no. 6 (2003), 160.

<sup>18</sup> EC – Conditions for the Granting of Tariff Preferences to Developing Countries, Report of the Panel, WT/DS246/R (1 December 2003) and Report of the Appellate Body (AB), WT/DS246/AB/R (7 April 2004).

<sup>19</sup> James Harrison, *Incentives for Development: The EC’s Generalized System of Preferences, India’s WTO Challenge and Reform*, 42 Common Market Law Review (2005), 1665.

<sup>20</sup> Decision on Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries of 28 November 1979, L/4903, paragraph 5.

<sup>21</sup> Decision on Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries of 28 November 1979, L/4903, paragraph 7.

<sup>22</sup> Lorand Bartels, *The WTO Enabling Clause and Positive Conditionality in the European Community’s GSP Program*, 6 Journal of International Economic Law, no. 2 (2003), 516. Also see footnote 192 of AB Report WT/DS246/AB/R which states that “the Enabling Clause is one of the “other decisions of the CONTRACTING PARTIES” within the meaning of paragraph 1(b)(iv) of the language of Annex 1A incorporating the GATT 1994 into the WTO Agreement.”

<sup>23</sup> Robert Howse, *India’s WTO Challenge to Drug Enforcement Conditions in the European Community Generalized System of Preferences: A Little Known Case with Major Repercussions for “Political” Conditionality in US Trade Policy*, 4 Chicago Journal of International Law, no. 2 (Fall 2003), 388.

The EC – Tariff Preferences case dealt with conditionalities in the European Union’s (EU’s<sup>24</sup>) GSP. It was the first case in the WTO in which the Enabling Clause was adjudicated.<sup>25</sup> It interpreted the meaning of non-discrimination and proved that the principle of non-discrimination, being the cornerstone of the multilateral trading system, must be complied with even in the exceptions, in this case the Enabling Clause. This means that there is really no exception to the principle of non-discrimination.

In this case, India challenged Regulation 2501/2001 of 10 December 2001 which laid down the following five schemes of preferences.

- (a) general arrangements,
- (b) special incentive arrangements for the protection of labour rights,
- (c) special incentive arrangements for the protection of the environment,
- (d) special arrangements for least developed countries, and
- (e) special arrangements to combat drug production and trafficking.<sup>26</sup>

The preferences under the general arrangements were granted to all developing countries whereas the fulfilment of certain conditions was required to benefit from additional preferences under the special arrangements. The special incentive arrangements for the protection of labour rights and the environment were so stringent that most developing countries did not even apply for them and only two succeeded in fulfilling the conditions.<sup>27</sup> The advantages under the last category ie the drug arrangements were granted to 11 countries<sup>28</sup> whose products benefited from zero tariffs whereas the products of other developing countries benefited from reduced tariffs or had to pay the entire tariff.<sup>29</sup> The EU felt that the 11 beneficiaries needed these preferences to

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<sup>24</sup> The EU was known as EC in the World Trade Organization (WTO) till 30 November 2009, see MEMBER INFORMATION The European Union and the WTO, available at:

[https://www.wto.org/english/thewto\\_e/countries\\_e/european\\_communities\\_e.htm](https://www.wto.org/english/thewto_e/countries_e/european_communities_e.htm), accessed 21 June 2016. The EC – Tariff Preferences case arose before 30 November 2009. In this article, the abbreviation EC will be used while referring to the aforementioned case and the abbreviation EU will be used in the remaining situations.

<sup>25</sup> Mitsuo Matsushita et al., *The World Trade Organization Law, Practice and Policy* (2<sup>nd</sup> ed., New York: Oxford University Press, 2006), p. 775; Ravindra Pratap, *WTO and Tariff Preferences India Wins Case, EC the Law*, XXXIX Economic and Political Weekly, no. 18 (1-7 May 2004), 1788. The EU GSP had been challenged in the past in the following cases in the WTO but they did not result in the adjudication of the Enabling Clause.

WT/DS154 EC – Measures Affecting Differential and Favourable Treatment of Coffee,

WT/DS209 EC – Measures Affecting Soluble Coffee,

WT/DS242 EC – GSP.

<sup>26</sup> Council Regulation (EC) No 2501/2001 of 10 December 2001 applying a scheme of generalised tariff preferences for the period from 1 January 2002 to 31 December 2004, OJ No. L 346, 31 December 2001, article 1.2.

<sup>27</sup> Gregory Shaffer and Yvonne Apea, *Institutional Choice in the Generalized System of Preferences Case: Who Decides the Conditions for Trade Preferences? The Law and Politics of Rights*, 39 *Journal of World Trade*, no. 6 (2005), 982.

<sup>28</sup> These countries were: Bolivia, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Honduras, Nicaragua, Panama, Peru, and Venezuela.

<sup>29</sup> See paragraphs 2.7-2.8 of Panel Report WT/DS246/R. The drug arrangements were laid down in article 10 of Regulation 2501/2001 which stated,

“1. Common Customs Tariff *ad valorem* duties on products which, according to Annex IV, are included in the special arrangements to combat drug production and trafficking referred to in Title IV and which originate in a country that according to Column I of Annex I benefits from those arrangements, shall be entirely suspended. For products of CN code 0306 13, the duty shall be reduced to a rate of 3,6 %.

stimulate their economic growth and improve their commercial possibilities so that the citizens of these countries would abandon the manufacture of illicit drugs and take up the manufacture of licit products instead.<sup>30</sup>

In 2001, the EU added Pakistan as the beneficiary of its additional preferences under the drug arrangements. The European Commission acknowledged that the EU granted additional preferential market access to Pakistani textiles and clothing to reward Pakistan for its position against the Taliban and also to gain access to the Pakistani market.<sup>31</sup> The grant of additional preferences to Pakistani textiles and clothing led to a distortion of the conditions of competition between India and Pakistan. It, thus, had a negative impact on India’s exports since India and Pakistan were competitors in the export of textiles and clothing to the EU.<sup>32</sup> Thus, developing countries such as India that lost market access paid for increased market access for other developing countries such as Pakistan.<sup>33</sup> Therefore, greater trade preferences can benefit a country at the cost of its competitor. Thus, increased market access can eradicate the problem of drugs in a country but reduced market access can increase the same problem in another country. Obviously, the aim of the Enabling Clause is not to transfer the problems of one country to another but this is exactly what the drug arrangements led to.<sup>34</sup>

India challenged the drug arrangements arguing that they violated the MFN treatment principle and were not justified by the Enabling Clause because its footnote 3<sup>35</sup> prevented the GSP donors from granting non-identical preferences to their beneficiaries. Moreover, paragraphs 2(a)<sup>36</sup> and 3(c)<sup>37</sup> referred to all developing countries. Since paragraph 2(a) did not allow donors to select their beneficiaries, preferences could not vary due to the needs of developing countries.

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2. Common Customs Tariff specific duties on products referred to in paragraph 1 shall be entirely suspended, except for products for which Common Customs Tariff duties also include *ad valorem* duties. For products of CN codes 1704 10 91 and 1704 10 99, the specific duty shall be limited to 16 % of the customs value.”

<sup>30</sup> Request for a WTO Waiver, New EC Special Tariff Arrangements to Combat Drug Production and Trafficking, G/C/W/328, 24 October 2001, paragraph 3.

<sup>31</sup> EU Response to the 11 September: European Commission action (Brussels, 12 March 2002), MEMO/02/53, available at: <[http://europa.eu/rapid/press-release\\_MEMO-02-53\\_en.htm](http://europa.eu/rapid/press-release_MEMO-02-53_en.htm)>, accessed 25 June 2016 and EU Response to the 11 September: European Commission action (Brussels, 3 June 2002), MEMO/02/122, available at: <[http://europa.eu/rapid/press-release\\_MEMO-02-122\\_en.htm](http://europa.eu/rapid/press-release_MEMO-02-122_en.htm)>, accessed 25 June 2016.

<sup>32</sup> Biswajit Dhar and Abhik Majumdar, *The India-EC GSP Dispute: The Issues and the Process*, pp. 3-7, available at: <<http://www.ictsd.org/downloads/2008/06/dhar.pdf>>, accessed 26 June 2016.

<sup>33</sup> Ravindra Pratap, *WTO and Tariff Preferences India Wins Case, EC the Law*, XXXIX Economic and Political Weekly, no. 18 (1-7 May 2004), 1788.

<sup>34</sup> Biswajit Dhar and Abhik Majumdar, *The India-EC GSP Dispute: The Issues and the Process*, p. 19, available at: <<http://www.ictsd.org/downloads/2008/06/dhar.pdf>>, accessed 26 June 2016.

<sup>35</sup> This footnote states, “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 18S/24).”

<sup>36</sup> This paragraph states, “The provisions of paragraph 1 apply to the following: [...] (a) Preferential tariff treatment accorded by developed contracting parties to products originating in developing countries in accordance with the Generalized System of Preferences.”

<sup>37</sup> This paragraph states, “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.”

So India’s argument was that developing countries had not given up on the MFN treatment principle which applied even when preferences were granted thus preventing donors from distinguishing between beneficiaries. So India was arguing that the principle of non-discrimination applies even in the exceptions. Normally, the word “discrimination” carries a negative connotation and means unjustified distinction. But India was arguing that any distinction, even if justified, amounted to discrimination and that GSP schemes must benefit all developing countries, without differentiation, to be protected by the Enabling Clause.

The EU argued that the Enabling Clause excluded the application of the MFN treatment principle. It stated that the drug arrangements were covered by paragraph 2(a) of the Enabling Clause instead of by the MFN treatment principle. It also argued that “non discriminatory” in footnote 3 of the Enabling Clause did not require the grant of identical preferences and allowed distinctions based on objective criteria such as developing countries’ needs. Moreover, paragraph 2(a) did not mention “all” developing countries which was confirmed by paragraph 3(c) which allowed preferences suited to the needs of developing countries.

Despite the important stakes India had in this case, Pascal Lamy, who was the European Trade Commissioner at that time, remarked that India did not need preferences suggesting that India would not benefit from the case.<sup>38</sup> However, India did not bring the case only due to economic reasons but because this case raised a systemic question – that of conditionalities in the GSP. Conditionality can be defined as the grant of benefits subject to the beneficiary meeting certain conditions. However, it carries a stronger meaning, as a mechanism to bring about policy reform in the beneficiaries or to impose policies which the beneficiary would not choose voluntarily.<sup>39</sup> In the World Bank, it implies provision of financial support to beneficiaries in return for implementation of structural changes.<sup>40</sup> In other words, conditionality is related to power since the balance of power between the donor and beneficiaries is important.<sup>41</sup>

The EU provides additional trade preferences to countries that comply with certain conditions. The EU’s rationale behind this is that “economic benefits are privileges to be granted to developing countries that comply with democratic principles and human rights, and to be withdrawn from those that do not.”<sup>42</sup> However, the EU does not include human rights and democracy conditionalities in its relations with developed countries.<sup>43</sup> Of course, these relations

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<sup>38</sup> Gregory Shaffer and Yvonne Apea, “GSP Programmes and Their Historical-Political-Institutional Context”, in Thomas Cottier et al. (eds.), *Human Rights and International Trade* (Oxford: Oxford University Press, 2005), p. 501, footnote 51.

<sup>39</sup> Oliver Morrissey, “Alternatives to Conditionality in Policy-Based Lending”, in Stefan Koeberle et al. (eds.), *Conditionality Revisited Concepts, Experiences, and Lessons* (Washington DC: The World Bank, 2005), p. 237.

<sup>40</sup> Stefan G. Koeberle, *Should Policy-Based Lending Still Involve Conditionality?*, 18 *The World Bank Observer*, no. 2 (Autumn 2003), 251.

<sup>41</sup> Patrick Watt, “Partnerships in Policy-Based Learning”, in Stefan Koeberle et al. (eds.), *Conditionality Revisited Concepts, Experiences, and Lessons* (Washington DC: The World Bank, 2005), p. 249.

<sup>42</sup> Lorand Bartels, *The Application of Human Rights Conditionality in the EU’s Bilateral Trade Agreements and other Trade Arrangements with Third Countries*, Directorate-General for External Policies of the Union, European Parliament, 2008, EXPO-B-INTA-2008-57 PE 406.991, p. 1.

<sup>43</sup> Lorand Bartels, *The Application of Human Rights Conditionality in the EU’s Bilateral Trade Agreements and other Trade Arrangements with Third Countries*, Directorate-General for External Policies of the Union, European Parliament, 2008, EXPO-B-INTA-2008-57 PE 406.991, p. 3.

exclude the GSP. But the EU’s difference in treatment of developing and developed countries shows that conditionalities are related to power.

India’s complaint raised two related questions. The first question related to the type of differentiation authorised – preferences granted to beneficiaries must be identical or is it possible to distinguish between them on the basis of different criteria?<sup>44</sup> The second question related to the status of footnote 3 in the Enabling Clause – was it binding and how to interpret it?<sup>45</sup>

The Panel found that the drug arrangements violated the MFN treatment principle and were not justified under paragraph 2(a) of the Enabling Clause. It also found that the term “non discriminatory” in footnote 3 of the Enabling Clause required the grant of identical preferences, without differentiation, to all developing countries; however, it allowed *a priori* limitations.<sup>46</sup> Additionally, it found that the term “developing countries” in paragraph 2(a) of the Enabling Clause referred to all developing countries but allowed *a priori* limitations.<sup>47</sup> The Panel referred to the UNCTAD Resolution 21 (II) to support its finding that the term “non discriminatory” meant a complete absence of distinction including on the basis of objective criteria. In fact, it found no objective criteria to distinguish between different development needs such as drug trafficking, poverty or poor education etc.<sup>48</sup>

The EU appealed and argued that the term “non discriminatory” obliged members to grant objective preferences because paragraph 3(c) required a response to the needs of developing countries. Moreover, paragraph 2(a) did not refer to all developing countries since paragraph 3(c) allowed objective distinctions.

The AB found that the term “non discriminatory” in footnote 3 of the Enabling Clause constituted an obligation and that GSP schemes would have to be non-discriminatory to be justified under paragraph 2(a) of the Enabling Clause.<sup>49</sup> However, the term “non discriminatory” did not require the grant of identical preferences.<sup>50</sup> Moreover, the term “developing countries” in paragraph 2(a) of the Enabling Clause did not refer to all developing countries.<sup>51</sup> The AB also stated that different developing countries could have different development needs susceptible of changing because development did not happen in a uniform manner in all developing countries.<sup>52</sup> It continued in the same vein by stating that developing countries could have different needs in accordance with their levels of development and particular circumstances.<sup>53</sup> The AB referred to

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<sup>44</sup> Gene M. Grossman and Alan O. Sykes, “European Communities – Conditions for the Granting of Tariff Preferences to Developing Countries (WT/DS246/AB/R)”, in Henrik Horn and Petros C. Mavroidis (eds.), *The WTO Case Law of 2003*, The American Law Institute Reporters' Studies (New York: Cambridge University Press, 2006), p. 221.

<sup>45</sup> Lorand Bartels, “The Appellate Body Report in *European Communities-Conditions for the Granting of Tariff Preferences to Developing Countries* and its Implications for Conditionality in GSP Programmes”, in Thomas Cottier et al. (eds.), *Human Rights and International Trade* (Oxford: Oxford University Press, 2005), p. 465.

<sup>46</sup> See paragraph 7.116 of Panel Report WT/DS246/R.

<sup>47</sup> See paragraph 78 of AB Report WT/DS246/AB/R.

<sup>48</sup> See paragraph 7.103 of Panel Report WT/DS246/R.

<sup>49</sup> See paragraph 148 of AB Report WT/DS246/AB/R.

<sup>50</sup> See paragraph 156 of AB Report WT/DS246/AB/R.

<sup>51</sup> See paragraphs 175-176 of AB Report WT/DS246/AB/R.

<sup>52</sup> See paragraph 160 of AB Report WT/DS246/AB/R.

<sup>53</sup> See paragraph 161 of AB Report WT/DS246/AB/R.

the Preamble to the WTO Agreement, which refers to the needs of members at different levels of economic development, to support its finding.<sup>54</sup>

The AB used paragraph 3(c) of the Enabling Clause as context to interpret its footnote 3<sup>55</sup> and stated that “we read paragraph 3(c) as authorizing preference-granting countries to “respond positively” to “needs” that are *not* necessarily common or shared by all developing countries. Responding to the “needs of developing countries” may thus entail treating different developing country beneficiaries differently.<sup>56</sup>” “In granting such differential tariff treatment, however, preference-granting countries are required, by virtue of the term “non-discriminatory”, to ensure that identical treatment is available to all similarly-situated GSP beneficiaries, that is, to all GSP beneficiaries that have the “development, financial and trade needs” to which the treatment in question is intended to respond.<sup>57</sup>”

Applying this criterion to the drug arrangements, the AB found that they were not available to all the beneficiaries of the GSP which were facing the problem of drug production and trafficking. The drug arrangements were limited to 12 developing countries and indicated neither the manner of selecting the beneficiaries nor the elements to determine the effect of the drug problem. There was no way to add other countries as beneficiaries of the arrangements. Furthermore, there were no criteria to distinguish beneficiaries of drug arrangements from other beneficiaries of the EU GSP. The drug arrangements did not lay down the criteria to remove beneficiaries. This meant that a beneficiary could continue to benefit from the drug arrangements irrespective of whether or not they resolved the drug problem in it.<sup>58</sup> This would certainly not be very encouraging for the development of developing countries facing drug problems but not benefiting from the drug arrangements. Moreover, the Regulation did not state the method of evaluating the drug arrangements’ response to the drug problems. This shows that the drug arrangements were opaque and were applied in an opaque as well as discriminatory fashion. Additionally, the EU had asked for a waiver from the MFN treatment principle because the drug arrangements benefited the products of 12 countries only.<sup>59</sup> Therefore, the AB did not agree with the EU that all developing countries were potential beneficiaries of the drug arrangements. Consequently, the EU was unable to prove that the drug arrangements satisfied the requirement of “non discriminatory” in footnote 3 and that they were justified under paragraph 2(a) of the Enabling Clause.<sup>60</sup>

### **Evaluation of the EC – Tariff Preferences Case**

This case raised a number of difficult questions but also left quite a few of them unanswered thus leading to uncertainty regarding GSP schemes. The main reason for this is that the Enabling Clause is ambiguous and this was acknowledged by the Panel and the AB. In fact, it does not

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<sup>54</sup> See paragraph 161 of AB Report WT/DS246/AB/R.

<sup>55</sup> See paragraph 130 of AB Report WT/DS246/AB/R.

<sup>56</sup> See paragraph 162 of AB Report WT/DS246/AB/R.

<sup>57</sup> See paragraph 173 of AB Report WT/DS246/AB/R.

<sup>58</sup> See paragraphs 180-183 of AB Report WT/DS246/AB/R.

<sup>59</sup> Request for a WTO Waiver, New EC Special Tariff Arrangements to Combat Drug Production and Trafficking, G/C/W/328, 24 October 2001, paragraph 2.

<sup>60</sup> See paragraphs 186-190 of AB Report WT/DS246/AB/R.

provide definitions of the terms “non discriminatory” and “developing countries.” The Enabling Clause refers neither to all developing countries nor to particular developing countries.<sup>61</sup>

Like any decision, this one also has its pros and cons. Consequently, there have been varied reactions to the case since it was important for GSP donors as well as for beneficiaries. Some developing countries felt the AB’s finding would fragment their unity while others felt it reflected the diversity among the developing countries.<sup>62</sup> The decision in this case can be perceived as disadvantageous to developing countries or as a compromise between different interests.<sup>63</sup> Brazil felt that the AB legitimised the use of GSP as a tool of foreign policy.<sup>64</sup> It can also be said that India won the case since the drug arrangements were struck down, but the interpretation of the law was in the EU’s favour.<sup>65</sup> Both the parties expressed their reactions to the decision. India expressed its dissatisfaction at the decision by stating that “the Appellate Body in this case had disregarded the ordinary meaning of the term “non-discriminatory”, as well as the relevant WTO jurisprudence, and had also failed to conduct an analysis of this term in the context of Article I.1 of the GATT 1994. It had then gone on to interpret the term “non-discriminatory” solely on the basis of paragraph 3(c) [of] the Enabling Clause. India had expressed its concern about the lack of adequate legal basis in the Appellate Body’s analysis for determining that developing countries could be treated differently by GSP donors, and the fear of a return to the era of special preferences that had prevailed before the GSP had been installed in the trading system.<sup>66</sup>” Meanwhile, the EU stated in a press release that the decision was a victory for GSP donors, including the EU, wanting to respond positively to particular needs of sub-groups of similarly-situated developing countries.<sup>67</sup>

It may be useful to examine the concept of discrimination since the entire case hinged on it. Non-discrimination in the WTO is not a linear concept. It varies from one legal provision to another.<sup>68</sup> Moreover, conditionalities can lead to discrimination but can also be non-discriminatory. Thus, discrimination and conditionality are not synonymous. The condition can lead to discrimination when applied in a uniform manner to all the beneficiaries. The requirement of fulfilling objective minimum conditions can be discriminatory since certain potential beneficiaries/developing countries not in a position to fulfil them may not benefit from the additional preferences. This

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<sup>61</sup> Gene M. Grossman and Alan O. Sykes, *A preference for development: the law and economics of GSP*, 4 World Trade Review, no. 1 (2005), 52-53.

<sup>62</sup> Sonia E. Rolland, *Development at the World Trade Organization* (Oxford: Oxford University Press, 2012), p. 159.

<sup>63</sup> Biswajit Dhar and Abhik Majumdar, *The India-EC GSP Dispute: The Issues and the Process*, pp. 22-23, available at: <<http://www.ictsd.org/downloads/2008/06/dhar.pdf>>, accessed 26 June 2016.

<sup>64</sup> Gregory Shaffer and Yvonne Apea, *Institutional Choice in the Generalized System of Preferences Case: Who Decides the Conditions for Trade Preferences? The Law and Politics of Rights*, 39 Journal of World Trade, no. 6 (2005), 1004.

<sup>65</sup> Ravindra Pratap, *WTO and Tariff Preferences India Wins Case, EC the Law*, XXXIX Economic and Political Weekly, no. 18 (1-7 May 2004), 1788.

<sup>66</sup> Minutes of Meeting held on 20 July 2005, Dispute Settlement Body (DSB), WT/DSB/M/194, 26 August 2005, paragraph 32.

<sup>67</sup> Inde / OMC - SPG: l’OMC confirme qu’il est possible d’opérer une différenciation entre les pays en développement (Brussels, 7 April 2004), IP/04/476, available at : <[europa.eu/rapid/press-release\\_IP-04-476\\_fr.pdf](http://europa.eu/rapid/press-release_IP-04-476_fr.pdf)>, accessed 26 June 2016.

<sup>68</sup> Robert Howse, *India’s WTO Challenge to Drug Enforcement Conditions in the European Community Generalized System of Preferences: A Little Known Case with Major Repercussions for “Political” Conditionality in US Trade Policy*, 4 Chicago Journal of International Law, no. 2 (Fall 2003), 397.

means that the capacity of the potential beneficiaries to fulfil the conditions must be taken into account.<sup>69</sup> Thus, non-discrimination includes treating unequals unequally.<sup>70</sup> Oppenheim’s International Law Treatise explains discrimination as treating differently those who are in the same situation or treating in the same way those who are in different situations.<sup>71</sup> Thus, countries situated differently can be treated differently. The AB also clarified this when it stated that similarly-situated beneficiaries should be treated alike. This is also highlighted in article XX of the GATT<sup>72</sup> which allows non-discriminatory conditions, article 2.3 of the Agreement on the Application of Sanitary and Phytosanitary Measures,<sup>73</sup> and paragraph 2(d) of the Enabling Clause.<sup>74</sup>

The AB struck down the drug arrangements due to lack of transparency but it could be argued that the Enabling Clause does not require transparency in the administration of GSP schemes because a lack of transparency does not necessarily amount to discrimination even in the case of a closed list as long as the GSP donor has correctly evaluated the needs of beneficiaries and the responses to those needs.<sup>75</sup> However, this argument ignores the fact that closed lists cannot exist in case of proper evaluation of needs and responses to those needs which can only be made by practising transparency. The element of discrimination could have been removed by following this procedure. Since it was not followed, the drug arrangements were discriminatory because of lack of transparency.

One of the difficulties in implementing the criteria laid down by the AB will be to find out if potential beneficiaries are “similarly-situated” since the AB did not provide a definition of the term.

The AB’s decision allows more freedom to donors to distinguish between beneficiaries as long as these distinctions fulfil the requirements laid down in the Enabling Clause<sup>76</sup> as interpreted by the AB. The AB stated that these distinctions must be based on objective criteria such as those recognised in the WTO Agreement or in international instruments.<sup>77</sup> As a consequence, the AB enhanced the possibility for donor countries to add conditions, including non-economic ones.

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<sup>69</sup> Lorand Bartels, *The WTO Enabling Clause and Positive Conditionality in the European Community’s GSP Program*, 6 *Journal of International Economic Law*, no. 2 (2003), 524.

<sup>70</sup> James Harrison, *GSP conditionality and non-discrimination*, 9 *International Trade Law & Regulation*, no. 6 (2003), 164.

<sup>71</sup> See footnote 318 of AB Report WT/DS246/AB/R.

<sup>72</sup> This article states, “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 by any contracting party of measures...”

<sup>73</sup> This article states, “Members shall ensure that their sanitary and phytosanitary measures do not arbitrarily or unjustifiably discriminate between Members where identical or similar conditions prevail...”

<sup>74</sup> This paragraph states, “The provisions of paragraph 1 apply to the following: [...] (d) Special treatment on the least developed among the developing countries in the context of any general or specific measures in favour of developing countries.”

<sup>75</sup> Lorand Bartels, “The Appellate Body Report in *European Communities-Conditions for the Granting of Tariff Preferences to Developing Countries* and its Implications for Conditionality in GSP Programmes”, in Thomas Cottier et al. (eds.), *Human Rights and International Trade* (Oxford: Oxford University Press, 2005), pp. 483-484.

<sup>76</sup> James Harrison, *Incentives for Development: The EC’s Generalized System of Preferences, India’s WTO Challenge and Reform*, 42 *Common Market Law Review* (2005), 1674.

<sup>77</sup> See paragraph 163 of AB Report WT/DS246/AB/R.

This is obviously not favourable from the point of view of potential beneficiaries which cannot always fulfil these conditions.

The AB simply assumed that the criteria it referred to were objective and did not define the term “objective.” It did not specify who bore the burden of proof to prove the objectivity of the criteria.<sup>78</sup> Also, it did not specify the method of application of the objective criteria. Should they be applied to the entire economy of the potential beneficiary or to its sectors or to international standards such as the UN Human Development Index?<sup>79</sup> This allows the GSP donor to select the method of application of the objective criteria.

Also, the freedom to objectively distinguish allowed by the AB may be misused to favour allies<sup>80</sup> or pressurise developing countries in multilateral or bilateral negotiations. Donors may include these conditions in bilateral agreements with developing countries<sup>81</sup> and this would exclude recourse to WTO dispute settlement.

Moreover, there are a number of needs/problems such as health, education etc that need to be resolved and it may be discriminatory if the EU only grants preferences to resolve drug problems as opposed to other needs.<sup>82</sup> This is because unfettered discretion to choose the needs to be addressed may amount to *de facto* discrimination among beneficiaries, thus highlighting the weakness of the criteria laid down by the AB. It did not require a GSP donor to respond to all possible development, financial, and trade needs of potential beneficiaries.<sup>83</sup> This leads to the following questions.

- (a) How to define a development, financial or trade need?
- (b) Do GSP donors have absolute discretion to choose the problems that they resolve?
- (c) How can the problem be quantified in order to be resolved?
- (d) Is exclusion of sensitive products from the benefits of GSP schemes not discriminatory?
- (e) Do these conditions not amount to a requirement of reciprocity?<sup>84</sup>

Additionally, the economic interests of beneficiaries evolve. A broad GSP scheme covering many products (espoused by the Panel<sup>85</sup>) allows the beneficiaries to shift to exporting newer products. A narrow GSP scheme tailored to similarly-situated beneficiaries does not allow the beneficiaries to shift to exporting newer products because this shift is governed by the GSP donor who might have an interest in maintaining the beneficiary in the existing position. Besides,

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<sup>78</sup> Sonia E. Rolland, *Development at the World Trade Organization* (Oxford: Oxford University Press, 2012), p. 162.

<sup>79</sup> Sonia E. Rolland, *Development at the World Trade Organization* (Oxford: Oxford University Press, 2012), p. 161.

<sup>80</sup> Gene M. Grossman and Alan O. Sykes, *A preference for development: the law and economics of GSP*, 4 *World Trade Review*, no. 1 (2005), 53-54.

<sup>81</sup> Stéphane de la Rosa, *Observations après le rapport du groupe spécial “Communautés européennes – conditions d’octroi de préférence tarifaires aux pays en développement”*. *Vers une remise en cause du SPG communautaire “à la carte” ?*, 15 *L’Observateur des Nations Unies* (Autumn - Winter 2003), 23.

<sup>82</sup> Robert Howse, *India’s WTO Challenge to Drug Enforcement Conditions in the European Community Generalized System of Preferences: A Little Known Case with Major Repercussions for “Political” Conditionality in US Trade Policy*, 4 *Chicago Journal of International Law*, no. 2 (Fall 2003), 400.

<sup>83</sup> Lorand Bartels, *The WTO Legality of the EU’s GSP+ Arrangement*, 10 *Journal of International Economic Law*, no. 4 (2007), 878.

<sup>84</sup> Gene M. Grossman and Alan O. Sykes, *A preference for development: the law and economics of GSP*, 4 *World Trade Review*, no. 1 (2005), 55-56.

<sup>85</sup> See paragraph 7.175 of Panel Report WT/DS246/R.

it is possible that this beneficiary that is unable make the shift is actually an inefficient producer of that product.<sup>86</sup>

Another consequence of the AB’s ruling is that GSP donors will determine whether or not a country is a developing country, a determination which is normally made by countries themselves. Potential beneficiaries will have to prove that they fulfil the conditions or that the conditions are unlawful. But the AB has not clarified if the potential beneficiary has to prove that it fulfils the conditions or that the GSP donor has to prove that the potential beneficiary does not fulfil the conditions.<sup>87</sup> These issues can be avoided in a GSP scheme without conditions.

Furthermore, there is a contradiction between the decision of the AB which makes “non discriminatory” a requirement and the Doha Decision on Implementation-related Issues and Concerns which states that preferences “should” be non-discriminatory.<sup>88</sup> Given the *de facto* rule of precedent that operates in WTO dispute settlement, it is possible that a future panel or AB would consider the decision in the present case. But the Doha Decision on Implementation-related Issues and Concerns may also be relevant under articles 31.3(a) and 31.3(b) of the Vienna Convention on the Law of Treaties 1969 (VCLT) which refer to subsequent agreement or practice of the parties regarding the interpretation of the treaty.<sup>89</sup>

Paragraph 3(a) of the Enabling Clause states that “[a]ny differential and more favourable treatment provided under this clause: (a) shall be designed to facilitate and promote the trade of developing countries.” If the GSP donors are allowed to distinguish between potential beneficiaries on shaky objective grounds, would they not be contradicting this paragraph? So is the AB’s interpretation in conformity with this paragraph?<sup>90</sup>

The AB stated that differentiation was allowed to respond to the needs of developing countries. The drug arrangements were not based on any criteria and were thus discriminatory. India’s argument that no distinction should be made between beneficiaries based on their needs would lead to discrimination because the grant of identical preferences to developing countries having different needs would not allow a response to these different needs thus leading to discrimination. Nevertheless, responding differently to different needs requires more complex laws.<sup>91</sup> Therefore, the AB’s approach is harder to implement compared with that of the Panel.

Footnote 3 and paragraph 3(c) were always present in the Enabling Clause but their status was ambiguous. By interpreting them as requirements, the AB has placed limits on the freedom of

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<sup>86</sup> Sonia E. Rolland, *Development at the World Trade Organization* (Oxford: Oxford University Press, 2012), p. 160.

<sup>87</sup> Sonia E. Rolland, *Development at the World Trade Organization* (Oxford: Oxford University Press, 2012), pp. 161-163.

<sup>88</sup> Doha Decision on Implementation-related Issues and Concerns adopted on 14 November 2001, WT/MIN(01)/17, 20 November 2001, paragraph 12.2.

<sup>89</sup> Robert Howse, *India’s WTO Challenge to Drug Enforcement Conditions in the European Community Generalized System of Preferences: A Little Known Case with Major Repercussions for “Political” Conditionality in US Trade Policy*, 4 *Chicago Journal of International Law*, no. 2 (Fall 2003), 392, footnote 28.

<sup>90</sup> Biswajit Dhar and Abhik Majumdar, *The India-EC GSP Dispute: The Issues and the Process*, p. 19, available at: <<http://www.ictsd.org/downloads/2008/06/dhar.pdf>>, accessed 26 June 2016.

<sup>91</sup> Steve Charnovitz et al., *Internet Roundtable The Appellate Body’s GSP decision*, 3 *World Trade Review*, no. 2 (2004), 264.

GSP donors to impose arbitrary conditions. These limits are necessary to avoid arbitrariness<sup>92</sup> as was manifest in the EC – Tariff Preferences case. Theoretically, the AB’s interpretation is more favourable to potential beneficiaries since it would allow the donors to respond to needs requiring additional preferences. In reality, it will depend on the beneficiaries’ capacity to fulfil the conditions.

This case will have an impact on negative or positive conditionalities in GSP schemes which are difficult to fulfil and which distinguish between similarly-situated beneficiaries. The AB stated that preferences should bring about a positive response to the needs of the beneficiary.<sup>93</sup> How would negative conditions bring about positive responses unless withdrawal of preferences is seen as contributing positively to the alleviation of a problem/need? So the AB’s interpretation might push donors to change from negative to positive conditionalities and lead to a decrease in reasons qualifying as needs justifying a distinction between beneficiaries.<sup>94</sup>

Certain scholars argue that the GSP will lead to *de facto* discrimination among beneficiaries since it is supposed to promote industrialisation through the export of manufactured goods. Other factors leading to discrimination are as follows: some beneficiaries are unfit to be recipients politically and sensitive domestic sectors of donors are to be protected.<sup>95</sup> By way of example, the GSP of the United States (US) uses geopolitical considerations and sensitivity of products to determine beneficiary status.<sup>96</sup> Moreover, GSP schemes introduced after the second meeting of the UNCTAD did have many conditions which were not outlawed by the Enabling Clause.<sup>97</sup> This means that donors had never accepted that their freedom to impose conditions would be constrained.<sup>98</sup> However, these arguments ignore the fact that the Enabling Clause failed to explicitly allow conditions in the GSP. In fact, the AB only interpreted paragraph 3(c) already present in the Enabling Clause. Other scholars argue that no conditions were envisaged when the GSP came about because it aimed at enhancing growth in developing countries by means of exports.<sup>99</sup> Moreover, these conditions demonstrate the donors’ desire to maintain unilateralism in the grant of preferences<sup>100</sup> and amount to disguised protectionism.<sup>101</sup> Importantly, these GSP

<sup>92</sup> Steve Charnovitz et al., *Internet Roundtable The Appellate Body’s GSP decision*, 3 World Trade Review, no. 2 (2004), 247.

<sup>93</sup> See paragraph 164 of AB Report WT/DS246/AB/R.

<sup>94</sup> Lorand Bartels, “The Appellate Body Report in *European Communities-Conditions for the Granting of Tariff Preferences to Developing Countries* and its Implications for Conditionality in GSP Programmes”, in Thomas Cottier et al. (eds.), *Human Rights and International Trade* (Oxford: Oxford University Press, 2005), p. 484.

<sup>95</sup> Gene M. Grossman and Alan O. Sykes, *A preference for development: the law and economics of GSP*, 4 World Trade Review, no. 1 (2005), 43.

<sup>96</sup> Gene M. Grossman and Alan O. Sykes, *A preference for development: the law and economics of GSP*, 4 World Trade Review, no. 1 (2005), 45.

<sup>97</sup> Gene M. Grossman and Alan O. Sykes, *A preference for development: the law and economics of GSP*, 4 World Trade Review, no. 1 (2005), 54.

<sup>98</sup> Robert Howse, *India’s WTO Challenge to Drug Enforcement Conditions in the European Community Generalized System of Preferences: A Little Known Case with Major Repercussions for “Political” Conditionality in US Trade Policy*, 4 Chicago Journal of International Law, no. 2 (Fall 2003), 395.

<sup>99</sup> Stéphane de la Rosa, *Observations après le rapport du groupe spécial “Communautés européennes – conditions d’octroi de préférence tarifaires aux pays en développement”. Vers une remise en cause du SPG communautaire “à la carte” ?*, 15 L’Observateur des Nations Unies (Autumn - Winter 2003), 4.

<sup>100</sup> Stéphane de la Rosa, *Observations après le rapport du groupe spécial “Communautés européennes – conditions d’octroi de préférence tarifaires aux pays en développement”. Vers une remise en cause du SPG communautaire “à la carte” ?*, 15 L’Observateur des Nations Unies (Autumn - Winter 2003), 16.

schemes containing conditionalities demonstrate an element of discrimination and reciprocity not envisaged by the UNCTAD Resolution 21 (II).<sup>102</sup> Most of the discriminatory characteristics in GSP schemes are not meant to promote social values and may be open to scrutiny after this case.<sup>103</sup> In fact, the EU had argued in this case that the drug arrangements were meant to protect European citizens from drugs, which proves that conditions in GSP schemes may not necessarily be for the benefit of the beneficiaries.

Additionally, donors question the validity of regulation of conditionalities in unilateral GSP schemes and might withdraw these schemes if restrictions are imposed on their freedom to impose conditions.<sup>104</sup> But the lack of regulation of conditionalities might lead to discriminatory preferences which existed before the UNCTAD.<sup>105</sup> It has been argued that developing countries should have anticipated these conditions because they help donors buy political support for GSP schemes in their territories.<sup>106</sup>

### **Suggestions for an Alternative Decision in/Rewriting the EC – Tariff Preferences Case**

In case the AB had been asked to decide on the WTO-legality of conditionalities, it was in a position to say that conditions should not be attached to GSP schemes because conditions would necessarily be discriminatory. This would not have amounted to legislation because India had argued that all potential beneficiaries should be treated alike. There could be two responses to this argument. The first is that all potential beneficiaries should be required to fulfil the same conditions irrespective of their ability to do so (since similarly-situated is not defined). This is the response given by the AB. The second is that no potential beneficiary should be required to fulfil any condition. In this second response, the AB could have compared paragraph 3(c) and footnote 3 of the Enabling Clause and could have concluded that modification of GSP schemes in accordance with paragraph 3(c) does not allow conduct which would be considered discriminatory under footnote 3. Thus, conditions, which are discriminatory by nature, would have been outlawed. Conditions are discriminatory by nature because (a) they ignore the

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<sup>101</sup> Stéphane de la Rosa, *Observations après le rapport du groupe spécial “Communautés européennes – conditions d’octroi de préférence tarifaires aux pays en développement”*. *Vers une remise en cause du SPG communautaire “à la carte” ?*, 15 L’Observateur des Nations Unies (Autumn - Winter 2003), 23.

<sup>102</sup> Gene M. Grossman and Alan O. Sykes, “European Communities – Conditions for the Granting of Tariff Preferences to Developing Countries (WT/DS246/AB/R)”, in Henrik Horn and Petros C. Mavroidis (eds.), *The WTO Case Law of 2003*, The American Law Institute Reporters’ Studies (New York: Cambridge University Press, 2006), p. 227.

<sup>103</sup> Robert Howse, *Back to Court After Shrimp/Turtle? Almost but not Quite Yet: India’s Short Lived Challenge to Labor and Environmental Exceptions in the European Union’s Generalized System of Preferences*, 18 American University International Law Review, no. 6 (2003), 1380.

Outside of the GSP, the EU continued to make payments to coup-ridden Mauritania in exchange for fishing opportunities. This shows the EU’s lack of faith in human rights issues, see Lorand Bartels, *The Application of Human Rights Conditionality in the EU’s Bilateral Trade Agreements and other Trade Arrangements with Third Countries*, Directorate-General for External Policies of the Union, European Parliament, 2008, EXPO-B-INTA-2008-57 PE 406.991, p. 4.

<sup>104</sup> Gene M. Grossman and Alan O. Sykes, *A preference for development: the law and economics of GSP*, 4 World Trade Review, no. 1 (2005), 42, 57, 63, 65.

<sup>105</sup> Gene M. Grossman and Alan O. Sykes, *A preference for development: the law and economics of GSP*, 4 World Trade Review, no. 1 (2005), 66.

<sup>106</sup> Gene M. Grossman and Alan O. Sykes, *A preference for development: the law and economics of GSP*, 4 World Trade Review, no. 1 (2005), 55.

different situations of beneficiaries and (b) the power relationship between the donor and the beneficiary is asymmetrical. So this response would confirm India’s argument that all potential beneficiaries should be treated alike. Also, the removal of non-economic conditions in trade schemes would be helpful in achieving economic development goals which were the initial reason for establishing the GSP.

Interpretations can also be suggested by applying the VCLT to interpret paragraph 3(c) and footnote 3 of the Enabling Clause. Article 3.2 of the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU) refers to the “customary rules of interpretation of public international law” to interpret WTO law. These customary rules have been codified in articles 31 to 33 of the VCLT. The WTO judicial instances have always relied on these articles to interpret WTO law. Of course, the use of these interpretative aids can lead to different findings.

Article 31.1 VCLT states that “[a] treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.” The WTO judicial instances have shown great enthusiasm for dictionaries to determine the ordinary meaning of treaty terms.<sup>107</sup> But can any dictionary define “modified” in paragraph 3(c) and “non discriminatory” in footnote 3 of the Enabling Clause as allowing conditionalities? The context of the terms of the treaty and object and purpose of the treaty can be found in the Preamble to the WTO Agreement which states that “[r]ecognizing that their relations in the field of trade and economic endeavour should be conducted with a view to raising standards of living, ensuring full employment and a large and steadily growing volume of real income and effective demand, and expanding the production of and trade in goods and services, while allowing for the optimal use of the world's resources in accordance with the objective of sustainable development, seeking both to protect and preserve the environment and to enhance the means for doing so in a manner consistent with their respective needs and concerns at different levels of economic development.” The AB did refer to developing countries at different levels of development as mentioned in the Preamble to the WTO Agreement to interpret footnote 3 of the Enabling Clause.<sup>108</sup> Conditionalities can be viewed as creating obstacles to or encouraging the achievement of the aforementioned goals. Beneficiaries need to be able to fulfil the conditionalities to benefit from these goals. Thus, conditionalities themselves are conditional on the capacity of the beneficiaries. In such a situation, the ordinary meaning of the terms “modified” and “non discriminatory” in their context and the object and purpose of the treaty would not allow conditionalities.

The chapeau of article 31.2 VCLT states that the context of a treaty includes its preamble and, thus, supports the aforementioned interpretation. Article 31.2(a) VCLT states that the context also includes “[a]ny agreement relating to the treaty which was made between all the parties in connexion with the conclusion of the treaty.” The Panel had ruled that the UNCTAD Resolution 21 (II) was such an agreement under article 31.2(a) and that it was context for interpreting the

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<sup>107</sup> The AB used the Oxford English Dictionary even in the EC – Tariff Preferences case, see generally AB Report WT/DS246/AB/R. Also see Joost Pauwelyn, *Reply to Joshua Meltzer*, 25 Michigan Journal of International Law (2003-2004), 925.

<sup>108</sup> See paragraph 161 of AB Report WT/DS246/AB/R.

Enabling Clause.<sup>109</sup> This Resolution makes no mention of conditionalities. The Enabling Clause, when interpreted in the context of this Resolution, would not allow conditionalities. Article 31.2(b) VCLT states that the context also includes “[a]ny instrument which was made by one or more parties in connexion with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.” The UNCTAD Resolution 21 (II) would be such an instrument effectively disallowing conditionalities under the Enabling Clause. This interpretation is also supported by the AB ruling in EC – Chicken Cuts in which the AB stated that the concept of context under article 31 is not limited to the treaty text as demonstrated by articles 31.2(a) and 31.2(b).<sup>110</sup> Thus, the context for interpreting the WTO Agreement (to which the GATT 1994, along with the Enabling Clause, is annexed) can be found outside it as well. The AB made this observation while stating that the Harmonised System, not part of WTO law, constituted context under article 31.2(a) for the interpretation of the schedules of members<sup>111</sup> which are WTO law as per article II.7 of GATT.<sup>112</sup> The AB arrived at this conclusion in view of the close connection between the Harmonised System and WTO law.<sup>113</sup> Applying this logic, there is a close connection between the UNCTAD Resolution 21 (II) and the 1971 GSP Waiver which is also referred to in footnote 3 of the Enabling Clause. Thus, this Resolution can be context for the interpretation of the Enabling Clause as stated by the Panel.

Article 32 VCLT states that the supplementary means of interpretation include “the preparatory work of the treaty and the circumstances of its conclusion.” The Panel ruled that the UNCTAD Resolution 21 (II) was preparatory work to interpret the Enabling Clause.<sup>114</sup> This would disallow conditionalities. In any case, article 32 provides a non-exhaustive list of the supplementary means of interpretation as highlighted by the AB in EC – Chicken Cuts.<sup>115</sup> Therefore, the Panel was only doing what was allowed in the VCLT.

As stated earlier, these articles can lead to different findings and it is possible to argue that the Preamble to the WTO Agreement would allow conditionalities. Moreover, it can also be argued that the UNCTAD Resolution 21 (II) did not outlaw conditionalities and, therefore, the Enabling Clause can be interpreted to allow them. However, the aim of the UNCTAD negotiations on GSP was to reduce discrimination in the existing preferences which was incorporated in the 1971 GSP Waiver and the Enabling Clause. But the Enabling Clause did not outlaw conditions which can lead to discrimination.<sup>116</sup> But it did not allow conditions either and this should be taken into account in a judicial proceeding.

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<sup>109</sup> See paragraphs 7.86-7.87 of Panel Report WT/DS246/R. Also see Jane Bradley, “The Enabling Clause and the Applied Rules of Interpretation”, in Thomas Cottier et al. (eds.), *Human Rights and International Trade* (Oxford: Oxford University Press, 2005), p. 505.

<sup>110</sup> See paragraph 195 of EC – Customs Classification of Frozen Boneless Chicken Cuts, Report of the AB, WT/DS269/AB/R (12 September 2005).

<sup>111</sup> See paragraph 199 of AB Report WT/DS269/AB/R.

<sup>112</sup> This article states, “The Schedules annexed to this Agreement are hereby made an integral part of Part I of this Agreement.”

<sup>113</sup> See paragraphs 194-199 of AB Report WT/DS269/AB/R.

<sup>114</sup> See paragraph 7.88 of Panel Report WT/DS246/R. Also see Jane Bradley, “The Enabling Clause and the Applied Rules of Interpretation”, in Thomas Cottier et al. (eds.), *Human Rights and International Trade* (Oxford: Oxford University Press, 2005), p. 505.

<sup>115</sup> See paragraph 283 of AB Report WT/DS269/AB/R.

<sup>116</sup> Gene M. Grossman and Alan O. Sykes, *A preference for development: the law and economics of GSP*, 4 World Trade Review, no. 1 (2005), 55.

Apart from these articles, the Preamble of the VCLT makes a mention of certain principles which have not been used by the WTO judicial instances in interpreting WTO law. These principles include the following.

“Affirming that disputes concerning treaties, like other international disputes, should be settled by peaceful means and in conformity with the principles of justice and international law [...] Having in mind the principles of international law embodied in the Charter of the United Nations, such as the principles of the equal rights and self-determination of peoples, of the sovereign equality and independence of all States, of non-interference in the domestic affairs of States, of the prohibition of the threat or use of force and of universal respect for, and observance of, human rights and fundamental freedoms for all.”

The question is whether these principles can be used by the WTO judicial instances to interpret the Enabling Clause. WTO law is part of public international law even in the absence of article 3.2 of the DSU<sup>117</sup> and “is not to be read in clinical isolation from public international law.”<sup>118</sup> Also, article 31.3(c) VCLT states that “[a]ny relevant rules of international law applicable in the relations between the parties” must be taken into account. Of course, WTO law would prevail over public international law in case of conflict between the two.<sup>119</sup> It has been argued that the principles mentioned in the Preamble of the VCLT are constitutional principles and have been enshrined in many instruments of the UN thus making them customary law requirements for the members of the UN and for the interpretation of treaties, including in WTO judicial proceedings.<sup>120</sup> Article 31.3(c) VCLT reflects the acceptance of these principles by all members of the UN.<sup>121</sup> In view of the fact that most members of the WTO are also members of the UN, this would imply that WTO law can be interpreted in light of the principles mentioned in the Preamble of the VCLT. In any case, the AB has inherent powers to administer justice but which it has not exercised.<sup>122</sup> But how would justice be defined? It could mean that conditions in GSP schemes should be imposed to benefit citizens of beneficiary countries. It could also mean that imposing conditions would impose unjust burdens on the beneficiary countries. Also, not giving additional preferences or taking away preferences when conditions are not fulfilled means citizens of beneficiary countries are deprived of employment opportunities. Moreover, a balance will have to be struck between the rights of states (sovereign equality, independence, and non-interference) and the human rights of citizens. This is because many developing countries may not be parties to many international instruments.<sup>123</sup> Even if rights of states can be ignored, the

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<sup>117</sup> Joost Pauwelyn, *How to Win a World Trade Organization Dispute Based on Non-World Trade Organization Law? Questions of Jurisdiction and Merits*, 37 *Journal of World Trade*, no. 6 (2003), 1001.

<sup>118</sup> See p. 17 of US – Standards for Reformulated and Conventional Gasoline, Report of the AB, WT/DS2/AB/R (29 April 1996).

<sup>119</sup> See paragraph 7.96 of Korea – Measures Affecting Government Procurement, Report of the Panel, WT/DS163/R (1 May 2000).

<sup>120</sup> Ernst-Ulrich Petersmann, *Need for a New Philosophy of International Economic Law and Adjudication*, 17 *Journal of International Economic Law*, no. 3 (September 2014), 640, 659.

<sup>121</sup> Ernst-Ulrich Petersmann, *Need for a New Philosophy of International Economic Law and Adjudication*, 17 *Journal of International Economic Law*, no. 3 (September 2014), 641.

<sup>122</sup> Ernst-Ulrich Petersmann, *Need for a New Philosophy of International Economic Law and Adjudication*, 17 *Journal of International Economic Law*, no. 3 (September 2014), 659.

<sup>123</sup> Asif Qureshi, “Interpreting WTO Agreements for the Development Objective”, in Victor Mosoti (ed.), *Towards a Development-Supportive Dispute Settlement System in the WTO*, Sustainable Development and Trade Issues, ICTSD Resource Paper no. 5 (Geneva: International Centre for Trade and Sustainable Development, March 2003), p. 103.

Enabling Clause should be interpreted to allow conditionalities only if they promote human rights and other associated rights. This would also take into account the meaning of the term “justice.” Furthermore, top-down approaches are not very effective in achieving their goals and bottom-up approaches pushed by citizens are preferable.<sup>124</sup> This would mean that conditionalities may not achieve their goals even if well-intentioned unless citizens of beneficiary countries push for change.

Also, the WTO judicial instances can come up with a set of rules to examine legitimate conditions in GSP schemes and resolve any disputes about them. This allows GSP donors to determine conditions unilaterally subject to justification of differential treatment of beneficiaries and judicial review. But the GSP donors may design schemes that fulfil their policy goals and comply with the AB’s requirements. Or they might have many conditions in their GSP schemes thus shifting benefits from one beneficiary to another. The beneficiaries may not challenge these conditions for usual reasons of resource insufficiency or political weight of GSP donors but also because they would be unsure of the result of the challenge due to the uncertainty created by the AB’s decision.<sup>125</sup>

These were suggested interpretations. In view of the existing interpretation given by the AB, the EU replaced the defaulting Regulation with another one.

### **Evaluation of the New European GSP+ Scheme**

The EU came up with Regulation 980/2005<sup>126</sup> to replace the previous Regulation 2501/2001. This was followed by Regulation 732/2008.<sup>127</sup> Article 1.2 of the two Regulations laid down the following three schemes.

- (a) a general arrangement,
- (b) a special incentive arrangement for sustainable development and good governance,
- (c) a special arrangement for least developed countries.

Article 1.2 of the currently applicable Regulation 978/2012<sup>128</sup> provides for the following schemes.

- (a) a general arrangement;
- (b) a special incentive arrangement for sustainable development and good governance (GSP+);  
and
- (c) a special arrangement for the least-developed countries (Everything But Arms (EBA)).

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<sup>124</sup> Ernst-Ulrich Petersmann, *Need for a New Philosophy of International Economic Law and Adjudication*, 17 *Journal of International Economic Law*, no. 3 (September 2014), 654, 667-668.

<sup>125</sup> Gregory Shaffer and Yvonne Apea, *Institutional Choice in the Generalized System of Preferences Case: Who Decides the Conditions for Trade Preferences? The Law and Politics of Rights*, 39 *Journal of World Trade*, no. 6 (2005), 1001-1004.

<sup>126</sup> Council Regulation (EC) No 980/2005 of 27 June 2005 applying a scheme of generalised tariff preferences, OJ No. L 169, 30 June 2005.

<sup>127</sup> Council Regulation (EC) No 732/2008 of 22 July 2008 applying a scheme of generalised tariff preferences for the period from 1 January 2009 to 31 December 2011 and amending Regulations (EC) No 552/97, (EC) No 1933/2006 and Commission Regulations (EC) No 1100/2006 and (EC) No 964/2007, OJ No. L 211, 6 August 2008.

<sup>128</sup> Regulation (EU) No 978/2012 of the European Parliament and of the Council of 25 October 2012 applying a scheme of generalised tariff preferences and repealing Council Regulation (EC) No 732/2008, OJ No. L 303, 31 October 2012.

The European Economic and Social Committee (EESC) stated that the special incentive arrangements in Regulation 2501/2001 for the protection of labour rights and of the environment have not been effective and should be withdrawn. It also stated that conditionalities will not be useful in achieving their aim unless sufficient preferences are granted.<sup>129</sup> Despite this, the EU came up with the aforementioned three Regulations containing a special incentive arrangement for sustainable development and good governance because the EU feels that it has absolute discretion to impose conditions on preferential trade.<sup>130</sup> In fact, the EU stated that it was clear that it should promote human rights, labour rights, environment, and good governance standards by means of the GSP+. <sup>131</sup> Apart from the GSP+, the Regulation also lays down the following vulnerability criteria.

- (a) The 7 largest GSP sections of a beneficiary’s exports to the EU must exceed 75% of its total exports to the EU during the last 3 consecutive years and
- (b) a beneficiary’s exports of particular products to EU must not exceed 2% of the EU’s imports of those products during the last 3 consecutive years.<sup>132</sup>

This does not fulfil the AB’s criteria of differentiating between beneficiaries on the basis of development, finance, and trade needs.<sup>133</sup> It is, thus, obvious that there is a lack of coherence and a contradiction in the trade and development policy of the EU.<sup>134</sup>

Despite various regulations coming and going, the special incentive arrangement for sustainable development and good governance known as the GSP+ has remained the same.<sup>135</sup> It aims to help countries most in need.<sup>136</sup> Developing countries wanting to benefit from it must fulfil the vulnerability criteria as well as ratify and effectively implement 27 international conventions on human rights, labour, environmental protection, the fight against drugs, and corruption.<sup>137</sup> Regulation 2501/2001 only referred to conventions on labour and sustainable management of

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<sup>129</sup> See paragraphs 3.3, 3.3.3, 6.6.2, and 7.4 of Opinion of the European Economic and Social Committee on the ‘generalised system of preferences (GSP),’ 2004/C 110/10, 30 April 2004.

<sup>130</sup> See paragraphs 6.6.2.3 and 6.6.5.1 of Opinion of the European Economic and Social Committee on the ‘generalised system of preferences (GSP),’ 2004/C 110/10, 30 April 2004.

<sup>131</sup> Revised EU trade scheme to help developing countries applies on 1 January 2014, European Commission Memo (Brussels, 19 December 2013), p. 3, available at: <[http://trade.ec.europa.eu/doclib/docs/2013/december/tradoc\\_152015.pdf](http://trade.ec.europa.eu/doclib/docs/2013/december/tradoc_152015.pdf)>, accessed 25 June 2016.

<sup>132</sup> See article 9.1(a) and paragraph 1 of Annex VII of Regulation 978/2012.

<sup>133</sup> Lorand Bartels, *The Application of Human Rights Conditionality in the EU’s Bilateral Trade Agreements and other Trade Arrangements with Third Countries*, Directorate-General for External Policies of the Union, European Parliament, 2008, EXPO-B-INTA-2008-57 PE 406.991, p. 16.

<sup>134</sup> See paragraph 4.9 of Opinion of the European Economic and Social Committee on the ‘generalised system of preferences (GSP),’ 2004/C 110/10, 30 April 2004.

<sup>135</sup> The only differences are the following.

- (a) Regulations 980/2005 and 732/2008 refer to the International Convention on the Suppression and Punishment of the Crime of Apartheid whereas Regulation 978/2012 does not refer to it.
- (b) Regulation 978/2012 refers to the UN Framework Convention on Climate Change whereas Regulations 980/2005 and 732/2008 do not refer to it.

See Annex VIII of Regulation 978/2012, and Annex III of Regulation 980/2005 and Regulation 732/2008.

<sup>136</sup> Revised EU trade scheme to help developing countries applies on 1 January 2014, European Commission Memo (Brussels, 19 December 2013), p. 1, available at: <[http://trade.ec.europa.eu/doclib/docs/2013/december/tradoc\\_152015.pdf](http://trade.ec.europa.eu/doclib/docs/2013/december/tradoc_152015.pdf)>, accessed 25 June 2016.

<sup>137</sup> See article 9(1) of Regulation 978/2012.

tropical forests.<sup>138</sup> Thus, the potential beneficiaries could choose from any of the three arrangements devoted to labour, environment, and drugs and fulfil only the requirements pertaining to the particular arrangement. In the GSP+, a beneficiary has to fulfil all the criteria. So the GSP+ introduced after the EC – Tariff Preferences case requires fulfilment of more conditions. Therefore, the GSP+ is more restrictive and even protectionist.<sup>139</sup> It is doubtful that many developing countries can fulfil these conditions.<sup>140</sup> Also, the list of conventions to be ratified and effectively implemented is a unilateral decision taken by the EU. How does the AB propose to regulate the objectivity or subjectivity in this decision? It is possible that the conventions are chosen to benefit certain countries. This shows that the AB’s dependence on international instruments is not all that helpful in eliminating discrimination.

On the face of it, this scheme is not discriminatory and opaque since all developing countries are eligible for preferences if they fulfil the criteria laid down. But all developing countries may not be in a position to fulfil all the criteria. Even the EESC has recognised that fulfilment of conditions entails high costs not necessarily offset by preferential treatment.<sup>141</sup> So a *de jure* non-discriminatory scheme may lead to *de facto* discrimination. Countries may have the same needs irrespective of their capacity to ratify and implement these conventions. Or, countries may have different needs but are required to ratify and implement the same conventions. It is, thus, arguable if the GSP+ entitles similarly-situated beneficiaries to similar preferences. In any case, beneficiaries are not necessarily similarly-situated because they ratify and implement the same conventions.<sup>142</sup> Each developing country may have different needs not necessarily reflected in multilateral instruments, especially those included in the GSP+. Thus, the GSP+ may not respond to the AB criterion that the preferences alleviate a need. So the AB and EU standard of defining a need in terms of ratification and implementation of conventions does not necessarily fulfil the aim of addressing the need through preferences, thus defeating their very purpose. According to the European Commission, the grant of additional preferences depends on an objective identification of the development needs of developing countries.<sup>143</sup> Are conditionalities requiring the ratification and implementation of international conventions an objective method of identifying a development, financial or trade need? According to the European Parliament, these requirements can create barriers to the trade of developing countries thus excluding them from

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<sup>138</sup> See articles 14.2 and 21.2 of Regulation 2501/2001.

<sup>139</sup> Lorand Bartels, *The Application of Human Rights Conditionality in the EU’s Bilateral Trade Agreements and other Trade Arrangements with Third Countries*, Directorate-General for External Policies of the Union, European Parliament, 2008, EXPO-B-INTA-2008-57 PE 406.991, p. 19.

<sup>140</sup> Gregory Shaffer and Yvonne Apea, *Institutional Choice in the Generalized System of Preferences Case: Who Decides the Conditions for Trade Preferences?* *The Law and Politics of Rights*, 39 *Journal of World Trade*, no. 6 (2005), 1006.

<sup>141</sup> See paragraph 3.3.2 of Opinion of the European Economic and Social Committee on the ‘generalised system of preferences (GSP),’ 2004/C 110/10, 30 April 2004.

<sup>142</sup> Minutes of Meeting held on 20 July 2005, DSB, WT/DSB/M/194, 26 August 2005, paragraph 33.

<sup>143</sup> See paragraph 5 of Communication from the Commission to the Council, the European Parliament and the European Economic and Social Committee Developing countries, international trade and sustainable development: the function of the Community’s generalised system of preferences (GSP) for the ten-year period from 2006 to 2015, Brussels, COM(2004) 461 final, 7 July 2004.

potential preferences.<sup>144</sup> Therefore, discrimination is still possible if the standards used to determine the eligibility of beneficiaries are not objective or are unjustifiably burdensome.<sup>145</sup> As much as a single arrangement might seem simpler, it requires the fulfilment of extensive criteria defined in terms of international conventions and agencies, which might make it onerous<sup>146</sup> for potential beneficiaries. Furthermore, a really backward country would find the fulfilment of these criteria unjustifiably burdensome as opposed to a more advanced country.<sup>147</sup> This shows that standardised conditionality for beneficiaries at different levels of development can lead to discrimination against which the criteria laid down by the AB in the EC – Tariff Preferences case does not provide a guarantee.

In US – Shrimps, the AB said that “[w]e believe that discrimination results not only when countries in which the same conditions prevail are differently treated, but also when the application of the measure at issue does not allow for any inquiry into the appropriateness of the regulatory program for the conditions prevailing in those exporting countries.<sup>148</sup>” So discrimination would result since the GSP+ requires potential beneficiaries to fulfil identical conditions irrespective of their different situations/capabilities.

Furthermore, WTO law itself shows the way forward when article XVII.3 of the General Agreement on Trade in Services dealing with national treatment states that “[f]ormally identical or formally different treatment shall be considered to be less favourable if it modifies the conditions of competition in favour of services or service suppliers of the Member compared to like services or service suppliers of any other Member.” So there is a recognition that formally identical treatment can lead to discrimination. In this sense, the complete absence of conditions from GSP schemes is identical treatment but it is less problematic than having conditions.

Another problematic issue is that the potential beneficiaries are required to fulfil the conditions before benefitting from the preferences.<sup>149</sup> This discriminates in favour of those potential beneficiaries which can incur such cost of fulfilling the conditions. This shortcoming may be removed by (a) granting preferences before requiring fulfilment of the conditions and by (b) introducing a time gap between the grant of preferences and fulfilment of conditions. Of course, this issue is not problematic if the conditions reflect customary international law.<sup>150</sup>

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<sup>144</sup> See paragraph 12 of P6\_TA(2004)0024 Generalised system of preferences European Parliament resolution on the Communication from the Commission to the Council, the European Parliament and the European Economic and Social Committee 'Developing countries, international trade and sustainable development: the function of the Community's generalised system of preferences (GSP) for the ten-year period from 2006 to 2015' (COM(2004)0461).

<sup>145</sup> James Harrison, *Incentives for Development: The EC's Generalized System of Preferences, India's WTO Challenge and Reform*, 42 Common Market Law Review (2005), 1678.

<sup>146</sup> James Harrison, *Incentives for Development: The EC's Generalized System of Preferences, India's WTO Challenge and Reform*, 42 Common Market Law Review (2005), 1681.

<sup>147</sup> James Harrison, *Incentives for Development: The EC's Generalized System of Preferences, India's WTO Challenge and Reform*, 42 Common Market Law Review (2005), 1682.

<sup>148</sup> See paragraph 165 of US – Import Prohibition of Certain Shrimp and Shrimp Products, Report of the AB, WT/DS58/AB/R (12 October 1998).

<sup>149</sup> See recital 13 of Regulation 978/2012.

<sup>150</sup> Lorand Bartels, *The WTO Legality of the EU's GSP+ Arrangement*, 10 Journal of International Economic Law, no. 4 (2007), 881-882.

Additionally, the GSP+ uses the conclusions of the monitoring bodies under the relevant conventions to determine if potential beneficiaries have effectively implemented the conventions and if they are eligible to receive preferences under the GSP+. <sup>151</sup> But the AB’s criteria did not account for the lack of clarity in the donors’ standard of review applicable to the conclusions of the monitoring bodies under the relevant conventions to determine if potential beneficiaries have effectively implemented the conventions. For example, the type of infraction of the conventions(s) leading to ineligibility of preferences is not known. <sup>152</sup>

So is the definition of conditionalities in a way that does not allow all potential beneficiaries to fulfil them not a form of discrimination? Moreover, this method of defining conditionalities is legal because it fulfils the criteria laid down by the AB. So the AB’s criteria are flawed and could lead to a return of discriminatory preferences that existed before the UNCTAD. <sup>153</sup>

The other question is whether conditionalities-based preferential trade actually responds to a development need which is not entirely economic in nature. For example, can preferential trade prevent genocide, in view of the requirement in the current GSP+ to ratify and implement the requisite convention? <sup>154</sup> So the GSP+ may be open to challenge if it does not alleviate the needs for which it was enacted. <sup>155</sup> According to the European Commission, there is a link between development and human rights, labour rights, environmental protection, and good governance. Additional preferences can respond positively to these specific needs. <sup>156</sup> However, the EESC stated that “there is no evidence that the special incentive arrangements for combating the production and trafficking of drugs, from which twelve countries have benefited, has had any impact whatsoever on the drug trade. <sup>157</sup>” It also stated that the GSP aims to develop the economies of beneficiaries instead of resolving all their problems. <sup>158</sup> This lack of consensus within the EU supports the argument of beneficiaries that these conditions are foreign to preferences devoted entirely to trade policy. <sup>159</sup> Also, the grant of additional preferences on the

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<sup>151</sup> See articles 9.1(b), 9.1(e), 9.1(f), 13, 14.3, and 15.6 of Regulation 978/2012. The previous Regulations laying down the GSP+ also depended on the review and monitoring mechanisms of the relevant conventions.

<sup>152</sup> Lorand Bartels, *The Application of Human Rights Conditionality in the EU’s Bilateral Trade Agreements and other Trade Arrangements with Third Countries*, Directorate-General for External Policies of the Union, European Parliament, 2008, EXPO-B-INTA-2008-57 PE 406.991, p. 8.

<sup>153</sup> Lorand Bartels, *The WTO Legality of the EU’s GSP+ Arrangement*, 10 *Journal of International Economic Law*, no. 4 (2007), 879.

<sup>154</sup> Lorand Bartels, *The Application of Human Rights Conditionality in the EU’s Bilateral Trade Agreements and other Trade Arrangements with Third Countries*, Directorate-General for External Policies of the Union, European Parliament, 2008, EXPO-B-INTA-2008-57 PE 406.991, p. 16.

<sup>155</sup> Lorand Bartels, *The WTO Legality of the EU’s GSP+ Arrangement*, 10 *Journal of International Economic Law*, no. 4 (2007), 881.

<sup>156</sup> See paragraph 6.5 of Communication from the Commission to the Council, the European Parliament and the European Economic and Social Committee Developing countries, international trade and sustainable development: the function of the Community’s generalised system of preferences (GSP) for the ten-year period from 2006 to 2015, Brussels, COM(2004) 461 final, 7 July 2004.

<sup>157</sup> See paragraph 6.6.2 of Opinion of the European Economic and Social Committee on the ‘generalized system of preferences (GSP),’ 2004/C 110/10, 30 April 2004.

<sup>158</sup> See paragraph 6.5 of Opinion of the European Economic and Social Committee on the ‘generalised system of preferences (GSP),’ 2004/C 110/10, 30 April 2004.

<sup>159</sup> Minutes of Meeting held on 20 July 2005, DSB, WT/DSB/M/194, 26 August 2005, paragraph 35; Biswajit Dhar and Abhik Majumdar, *The India-EC GSP Dispute: The Issues and the Process*, p. 21, available at: <<http://www.ictsd.org/downloads/2008/06/dhar.pdf>>, accessed 26 June 2016.

fulfilment of conditions implies granting preferences to countries that may not necessarily be in need of help and depriving those countries that cannot fulfil these conditions but may be really in need of help.<sup>160</sup> These countries may then question as to how these conditionalities respond to development needs. In any case, the success of GSP+ depends on the meaningful selection of beneficiaries, contingent on the use of relevant international conventions along with their monitoring and review mechanisms.<sup>161</sup> Also, potential beneficiaries’ acceptance of conventions does not necessarily imply acceptance of the use of conventions as conditionalities leading to discriminatory trade treatment.<sup>162</sup> Moreover, an important aspect of the GSP+ is that it does not benefit countries that have implemented the content of these international conventions without ratifying them.

The debate between the donors and beneficiaries can go on endlessly but there is some merit in the argument that the norms enshrined in international conventions can lead to development. The real question is whether or not conditions are the appropriate means of achieving this aim. Regarding labour standards conditionalities, certain scholars argue that trade liberalisation will lead to improvement in the condition of labour whereas other scholars argue that explicit linkages between trade policy and labour standards are required.<sup>163</sup> Others feel that the imposition of higher standards will lead to higher costs of hiring labour thus leading to employment of fewer workers; consequently, the higher standards will only benefit the fewer workers employed and not the large number of unemployed persons.<sup>164</sup> Therefore, despite the benefits of labour standards, the linkages between trade policy and labour standards should be approached keeping in mind the situation of employed and unemployed persons.<sup>165</sup> A lot has been written on the issue but there is no consensus on the utility of trade conditionality in promoting human and labour rights.<sup>166</sup> There are concerns that labour conditionalities are a result of protectionist interests in the developed world.<sup>167</sup> Withdrawal of the preferences will certainly

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<sup>160</sup> Lorand Bartels, *The WTO Legality of the EU’s GSP+ Arrangement*, 10 *Journal of International Economic Law*, no. 4 (2007), 877.

<sup>161</sup> James Harrison, *Incentives for Development: The EC’s Generalized System of Preferences, India’s WTO Challenge and Reform*, 42 *Common Market Law Review* (2005), 1680-1681.

<sup>162</sup> James Harrison, *Incentives for Development: The EC’s Generalized System of Preferences, India’s WTO Challenge and Reform*, 42 *Common Market Law Review* (2005), 1687, footnote 88.

<sup>163</sup> Philip Alston, ‘*Core Labour Standards’ and the Transformation of the International Labour Rights Regime*, 15 *European Journal of International Law*, no. 3 (2004), 471-472.

<sup>164</sup> Drusilla K. Brown et al., *Pros and Cons of Linking Trade and Labour Standards*, Discussion Paper no. 477, Research Seminar in International Economics, School of Public Policy, The University of Michigan, 6 May 2002, p. 20.

<sup>165</sup> Drusilla K. Brown et al., *Pros and Cons of Linking Trade and Labour Standards*, Discussion Paper no. 477, Research Seminar in International Economics, School of Public Policy, The University of Michigan, 6 May 2002, p. 21.

<sup>166</sup> James Harrison, *Incentives for Development: The EC’s Generalized System of Preferences, India’s WTO Challenge and Reform*, 42 *Common Market Law Review* (2005), 1683.

<sup>167</sup> Third World Intellectuals and NGOs Statement Against Linkage (TWIN-SAL), pp. 1-2, available at: <<https://www2.bc.edu/~anderson/twin-sal12.pdf>>, accessed 20 May 2016; Drusilla K. Brown et al., *Pros and Cons of Linking Trade and Labour Standards*, Discussion Paper no. 477, Research Seminar in International Economics, School of Public Policy, The University of Michigan, 6 May 2002, pp. 22-23; Opinion of the European Economic and Social Committee on the ‘generalised system of preferences (GSP),’ 2004/C 110/10, 30 April 2004, paragraph 4.4; Gregory Shaffer and Yvonne Apea, *Institutional Choice in the Generalized System of Preferences Case: Who Decides the Conditions for Trade Preferences? The Law and Politics of Rights*, 39 *Journal of World Trade*, no. 6 (2005), 990-991.

have negative effects on the populations of beneficiaries working in the export sectors.<sup>168</sup> This means that conditionalities have been imposed without proper research on their efficacy. However, such research will only help in devising more effective conditionalities, helpful for donors and beneficiaries.

### **What can GSP Donors Learn from the Discourse on Conditionalities in the Loans Granted by the World Bank?<sup>169</sup>**

Conditionalities are not unique to the GSP. They are used in various international transactions. For example, conditionalities are also part of the loans granted by the World Bank. The issues that arise in the case of the GSP+ have also arisen in the case of the World Bank. Suggestions have been made to resolve the problems that arise in the case of conditionalities imposed by the World Bank. These suggestions may provide some guidance in resolving the problems that arise in the case of conditionalities imposed in the GSP+.

In the World Bank, the impact of conditionalities on the performance of the recipient country has been mixed, tending towards the negative.<sup>170</sup> Moreover, the number of conditions imposed is very high.<sup>171</sup> This has also been observed in the case of the EU GSP+ requiring ratification and effective implementation of 27 conventions. Therefore, donors should limit the lending conditions. This would actually help in fulfilling the conditions since recipient governments can focus on the limited conditions instead of trying to fulfil the unimportant ones. Moreover, the recipient countries have limited resources and imposition of too many conditions is burdensome. Questions have also been raised on the imposition of conditions by donors thus undermining the idea of ownership of the good governance agenda in recipient countries. In fact, the major criticism of conditionality is its dictatorial or coercive element in imposing policies which makes for a weak partnership between donors and recipients because it deprives the latter of ownership in the choice of policies.<sup>172</sup> Also, there is no one single policy reform appropriate for all recipients. Thus, conditionality should differ according to the country context<sup>173</sup> since standardised conditionality would not take into account the situation prevailing in different countries and may lead to recipient countries losing ownership of the process. Moreover, studies prove that standardised conditionality in countries at different levels of development does not work. Furthermore, recipient countries may not be able to fulfil the conditions thus losing the

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<sup>168</sup> Lorand Bartels, *The Application of Human Rights Conditionality in the EU’s Bilateral Trade Agreements and other Trade Arrangements with Third Countries*, Directorate-General for External Policies of the Union, European Parliament, 2008, EXPO-B-INTA-2008-57 PE 406.991, p. 17.

<sup>169</sup> This section draws on Stefan Koeberle et al. (eds.), *Conditionality Revisited Concepts, Experiences, and Lessons* (Washington DC: The World Bank, 2005), 273 p. and Stefan G. Koeberle, *Should Policy-Based Lending Still Involve Conditionality?*, 18 *The World Bank Observer*, no. 2 (Autumn 2003), 249-273.

<sup>170</sup> Harold Bedoya, “Conditionality and Country Performance”, in Stefan Koeberle et al. (eds.), *Conditionality Revisited Concepts, Experiences, and Lessons* (Washington DC: The World Bank, 2005), p. 192. Also see Stefan G. Koeberle, *Should Policy-Based Lending Still Involve Conditionality?*, 18 *The World Bank Observer*, no. 2 (Autumn 2003), 252.

<sup>171</sup> Stefan G. Koeberle, *Should Policy-Based Lending Still Involve Conditionality?*, 18 *The World Bank Observer*, no. 2 (Autumn 2003), 252, 255.

<sup>172</sup> Oliver Morrissey, “Alternatives to Conditionality in Policy-Based Lending”, in Stefan Koeberle et al. (eds.), *Conditionality Revisited Concepts, Experiences, and Lessons* (Washington DC: The World Bank, 2005), p. 238.

<sup>173</sup> Stefan G. Koeberle, *Should Policy-Based Lending Still Involve Conditionality?*, 18 *The World Bank Observer*, no. 2 (Autumn 2003), 249, 256.

aid. However, it is possible to work with donors to reduce the number of conditionalities and to make them more specific. It is also possible to moderate the conditionalities according to the situation, for example, conditionalities could be different in a crisis situation.<sup>174</sup> Additionally, the recipient country’s institutional capacity should be taken into account as it determines the success of conditionalities.<sup>175</sup> The generality of these issues was reflected in a specific study on Vietnam which concluded that externally imposed conditionalities are not helpful. Therefore, an open dialogue between the donor and recipient country is required which should lead to the recipient country taking full ownership in the design and implementation of commitments.<sup>176</sup> Such open or policy dialogue is like a partnership in which donors persuade or convince recipient countries, instead of coercing them, to adopt certain policies. Such a dialogue is more likely to be successful and conditions could be used to support the dialogue.<sup>177</sup> These suggestions could be helpful for conditionalities in GSP schemes since they allow a dialogue between the GSP donor and potential beneficiaries. But the dialogue should not degenerate into a mechanism to pressurise the potential beneficiaries to comply with the conditions or to benefit the donors’ allies.

However, the fact remains that conditions may not be entirely effective, whether used independently or with dialogue. This is because governments are reluctant to implement policy reforms if the conditions are too restrictive and conditions are obviously inappropriate in cases where governments are keen on policy reform.<sup>178</sup> Furthermore, reform is a slow process and conditionalities try to impose quick reform ignoring local conditions, thus leading to failures. Consequently, donors should support policy reform instead of imposing it.<sup>179</sup> They can influence the policy reform in recipient countries by providing analytical research on the effects of alternative policies. Donor influence undermines ownership of policy reform but it is acceptable as long as the choice of policy reform, with the belief that it is the best choice, originates in the recipient country’s government. Thus, donors can provide information on policies but the choice should be left with the recipient country’s government. Additionally, donors should not provide standardised advice to all recipient governments unless it is the correct advice for that country. This allows recipient governments to experiment with policies and does away with the coercive nature of conditionalities since influence is not equivalent to imposing policies on the recipient governments. The other option is for the recipient governments to do their own research and come up with their choice of policy which would truly amount to ownership of the policy reform process. However, this is not necessarily required for policy reform. Also, recipient countries’ governments may be willing but unable to implement the chosen policies. In such a situation,

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<sup>174</sup> “Discussion Summary”, in Stefan Koeberle et al. (eds.), *Conditionality Revisited Concepts, Experiences, and Lessons* (Washington DC: The World Bank, 2005), pp. 225-226.

<sup>175</sup> Stefan G. Koeberle, *Should Policy-Based Lending Still Involve Conditionality?*, 18 *The World Bank Observer*, no. 2 (Autumn 2003), 266.

<sup>176</sup> Duong Duc Ung, “Policy-Based Lending and Conditionality: The Experience of Vietnam”, in Stefan Koeberle et al. (eds.), *Conditionality Revisited Concepts, Experiences, and Lessons* (Washington DC: The World Bank, 2005), p. 235.

<sup>177</sup> Oliver Morrissey, “Alternatives to Conditionality in Policy-Based Lending”, in Stefan Koeberle et al. (eds.), *Conditionality Revisited Concepts, Experiences, and Lessons* (Washington DC: The World Bank, 2005), p. 237.

<sup>178</sup> Oliver Morrissey, “Alternatives to Conditionality in Policy-Based Lending”, in Stefan Koeberle et al. (eds.), *Conditionality Revisited Concepts, Experiences, and Lessons* (Washington DC: The World Bank, 2005), p. 238.

<sup>179</sup> Oliver Morrissey, “Alternatives to Conditionality in Policy-Based Lending”, in Stefan Koeberle et al. (eds.), *Conditionality Revisited Concepts, Experiences, and Lessons* (Washington DC: The World Bank, 2005), p. 239.

donors should help in the implementation of the policies, by providing technical assistance.<sup>180</sup> In fact, the EU is funding a project since 1 October 2015 in 4 of its GSP+ beneficiaries to help them develop their capacity to comply with labour standards.<sup>181</sup> Going further, donors should grant the benefits even if the policy reform does not materialise.<sup>182</sup> As opposed to conditionalities, such a dialogue would be slow in bringing about reform but would be adapted to the recipient country’s environment.<sup>183</sup>

As stated earlier, conditions can be used to support dialogue. These conditions should be precise, clear, easy to monitor, and should reinforce or ensure that the recipient government actually follows the policy choices it made, instead of imposing policies on it. Also, conditions should be defined in terms of policy choices and not the goal the policy choice aims to achieve because goals may not be achieved even if the policy reform has been properly implemented. Besides this, conditions in various policy areas should be independent of each other to avoid conflict between them. But conditionalities in the traditional sense are not the best means of policy reform since they do not bring about change in the beliefs of the recipient governments. Change in beliefs can be brought about by starting with simpler reforms keeping in mind that the breadth of the reform programme is directly proportional to the level of development of the recipient country. It is not possible to have a dialogue with some countries such as failed states or authoritarian regimes. However, these are exceptions and do not reflect a shortcoming of the policy dialogue since traditional conditionalities would also be ineffective in such a situation.<sup>184</sup>

However, even though ownership is preferable to conditionalities, the issue of power remains unchanged. Thus, real partnerships should include shared objectives, mutual accountability, and two-way exchange of knowledge. However, these may not materialise if the balance of power is tilted in favour of the donor. Since the donors provide the benefits, they expect accountability from the recipient countries. However, the governments of recipient countries should also be accountable to their populations.<sup>185</sup> This is a significant issue when we talk of conditionalities, ownership, partnership or any kind of benefits because, ultimately, it is the population of the recipient country that must benefit from this process. Moreover, the presumption that donors have the knowledge on policies etc means that the exchange of knowledge is not a two-way

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<sup>180</sup> Oliver Morrissey, “Alternatives to Conditionality in Policy-Based Lending”, in Stefan Koeberle et al. (eds.), *Conditionality Revisited Concepts, Experiences, and Lessons* (Washington DC: The World Bank, 2005), pp. 241-242.

<sup>181</sup> These countries are: El Salvador, Guatemala, Mongolia, and Pakistan, see Generalised System of Preferences (GSP), EU-funded ILO project on labour rights in GSP+ countries, available at: <http://ec.europa.eu/trade/policy/countries-and-regions/development/generalised-scheme-of-preferences/>, accessed 25 June 2016. It may be noted that the EESC is helping developing countries build their capacity to respond to questionnaires, see paragraph 5.1 of Opinion of the European Economic and Social Committee on the ‘generalised system of preferences (GSP),’ 2004/C 110/10, 30 April 2004. It is these very countries that are expected to fulfil the conditionalities in the EU’s GSP+.

<sup>182</sup> Oliver Morrissey, “Alternatives to Conditionality in Policy-Based Lending”, in Stefan Koeberle et al. (eds.), *Conditionality Revisited Concepts, Experiences, and Lessons* (Washington DC: The World Bank, 2005), p. 242.

<sup>183</sup> Oliver Morrissey, “Alternatives to Conditionality in Policy-Based Lending”, in Stefan Koeberle et al. (eds.), *Conditionality Revisited Concepts, Experiences, and Lessons* (Washington DC: The World Bank, 2005), p. 244.

<sup>184</sup> Oliver Morrissey, “Alternatives to Conditionality in Policy-Based Lending” in Stefan Koeberle et al. (eds.), *Conditionality Revisited Concepts, Experiences, and Lessons* (Washington DC: The World Bank, 2005), pp. 244-246.

<sup>185</sup> Patrick Watt, “Partnerships in Policy-Based Learning”, in Stefan Koeberle et al. (eds.), *Conditionality Revisited Concepts, Experiences, and Lessons* (Washington DC: The World Bank, 2005), pp. 249-250.

process.<sup>186</sup> The same issue has been highlighted in the case of GSP+ conditionalities. The GSP donor makes an independent decision on the conditions to be fulfilled by the beneficiaries. These conditions may be in the form of ratification of various treaties etc but they certainly ignore the knowledge of the beneficiaries regarding their choices and needs<sup>187</sup> despite the EESC suggesting consultations with stakeholders in developing countries before introduction of a new GSP scheme.<sup>188</sup> Moreover, the ownership model is persuasion-based and sees benefits as steps to inducing reforms in the recipient country. This shows that it is a paternalistic model, as opposed to a partnership model.<sup>189</sup> The same problem arises in case of conditionalities in the GSP+ since they are far from ownership, not to mention partnership. However, this paternalism may not necessarily bring the desired reforms as seen in the case of the drug arrangements. Therefore, real partnership would require that donors remove reform-inducing conditions and standardised conditionality allowing for more diversity in the actual reforms. Donors should also be held accountable, especially to check if the benefits they grant are being diluted in other sectors<sup>190</sup> and if the implementation of the reforms suggested by the donors has led to any problems in the recipient country.<sup>191</sup> The same issues arise in case of conditionalities in the GSP+ where the EU has decided on a list of conventions to be ratified irrespective of the country that applies for the additional preferences and there is no scrutiny to find out if the grant of preferences is being weakened by other aspects of EU policy, including trade policy. This is despite the fact that civil society representatives have stated before the EESC that the benefits of the GSP are outweighed by non-tariff barriers.<sup>192</sup> This stance against conditionalities recognises that donors would like to have some conditions regarding the use of the benefits provided to the beneficiaries but does not support conditionalities imposing policy reform.<sup>193</sup>

## Conclusion

Developing countries are in a weaker bargaining position compared with the developed countries and can be played off against one and other.<sup>194</sup> Conditionalities are a useful tool for this purpose. As much as conditionalities are supposed to be helpful for the beneficiaries, they have been termed as a burden on beneficiaries, advancing developed country agendas.<sup>195</sup> As such,

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<sup>186</sup> Patrick Watt, “Partnerships in Policy-Based Learning”, in Stefan Koeberle et al. (eds.), *Conditionality Revisited Concepts, Experiences, and Lessons* (Washington DC: The World Bank, 2005), p. 250.

<sup>187</sup> Gregory Shaffer and Yvonne Apea, *Institutional Choice in the Generalized System of Preferences Case: Who Decides the Conditions for Trade Preferences? The Law and Politics of Rights*, 39 *Journal of World Trade*, no. 6 (2005), 998.

<sup>188</sup> See paragraph 7.10 of Opinion of the European Economic and Social Committee on the ‘generalised system of preferences (GSP),’ 2004/C 110/10, 30 April 2004.

<sup>189</sup> Patrick Watt, “Partnerships in Policy-Based Learning”, in Stefan Koeberle et al. (eds.), *Conditionality Revisited Concepts, Experiences, and Lessons* (Washington DC: The World Bank, 2005), p. 251.

<sup>190</sup> Patrick Watt, “Partnerships in Policy-Based Learning”, in Stefan Koeberle et al. (eds.), *Conditionality Revisited Concepts, Experiences, and Lessons* (Washington DC: The World Bank, 2005), pp. 251-252.

<sup>191</sup> “Discussion Summary”, in Stefan Koeberle et al. (eds.), *Conditionality Revisited Concepts, Experiences, and Lessons* (Washington DC: The World Bank, 2005), p. 255.

<sup>192</sup> See paragraph 4.2 of Opinion of the European Economic and Social Committee on the ‘generalised system of preferences (GSP),’ 2004/C 110/10, 30 April 2004.

<sup>193</sup> “Discussion Summary”, in Stefan Koeberle et al. (eds.), *Conditionality Revisited Concepts, Experiences, and Lessons* (Washington DC: The World Bank, 2005), p. 254.

<sup>194</sup> Gregory Shaffer and Yvonne Apea, *Institutional Choice in the Generalized System of Preferences Case: Who Decides the Conditions for Trade Preferences? The Law and Politics of Rights*, 39 *Journal of World Trade*, no. 6 (2005), 995.

developing countries fulfil the conditions only to benefit from preferences.<sup>196</sup> These conditions can be beneficial if both the donors and the beneficiaries implement them seriously. For this, developing countries should be convinced of the benefits of these policies. This will lead to ownership of the good governance agenda within their countries. Therefore, proper research into conditionalities should be conducted so that they are actually beneficial, thus leading to their acceptance internationally.<sup>197</sup> Human rights impact assessment of conditionalities should be conducted and they should be terminated if they worsen the human rights situation in the beneficiary.<sup>198</sup>

Additionally, the 1971 GSP Waiver recognises that “a principal aim of the CONTRACTING PARTIES is promotion of the trade and export earnings of developing countries for the furtherance of their economic development.<sup>199</sup>” This shows that (a) economic development is the end and (b) trade is a means to achieve that end. The Enabling Clause and the UNCTAD Resolution 21 (II) do not mention conditions. How, then, can non-economic conditions be a part of GSP schemes, especially when imposed by another country? Of course, economic development implies non-economic development but that is a domestic concern of the developing country or GSP beneficiary and should not be regulated by the GSP donor. Moreover, the AB should not contribute to the regulation of the beneficiary’s domestic non-economic development by the GSP donor. In this case, the AB encouraged such regulation by stating that international instruments may be used to define conditions. Of course, its aim was to make these conditions more objective, transparent, and rule-based. But it was also a way to allow freedom to GSP donors to distinguish between beneficiaries.<sup>200</sup>

It is hoped that the consequence of judicial outlawing of conditionalities will be that GSP schemes would no longer contain conditions. The counter argument to this is that the developed countries, the EU in this case, would withdraw the GSP schemes and this would be harmful to developing countries. However, the developed countries might only threaten withdrawal of GSP schemes because there might be domestic constituencies that do not want actual withdrawal. This threat could then be used as leverage in negotiations with potential beneficiaries.<sup>201</sup> So the outlawing of conditionalities might not be beneficial to developing countries.

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<sup>195</sup> Peter Sutherland et al., *The Future of the WTO Addressing institutional challenges in the new millennium*, Report by the Consultative Board to the Director-General Supachai Panitchpakdi (Geneva: WTO, 2004), pp. 24-25, paragraph 94; Gregory Shaffer and Yvonne Apea, *Institutional Choice in the Generalized System of Preferences Case: Who Decides the Conditions for Trade Preferences? The Law and Politics of Rights*, 39 *Journal of World Trade*, no. 6 (2005), 993.

<sup>196</sup> See Stefan G. Koeberle, *Should Policy-Based Lending Still Involve Conditionality?*, 18 *The World Bank Observer*, no. 2 (Autumn 2003), 252 making the same point in the case of the World Bank.

<sup>197</sup> James Harrison, *Incentives for Development: The EC’s Generalized System of Preferences, India’s WTO Challenge and Reform*, 42 *Common Market Law Review* (2005), 1688.

<sup>198</sup> Lorand Bartels, *The Application of Human Rights Conditionality in the EU’s Bilateral Trade Agreements and other Trade Arrangements with Third Countries*, Directorate-General for External Policies of the Union, European Parliament, 2008, EXPO-B-INTA-2008-57 PE 406.991, p. 20.

<sup>199</sup> See Waiver, Generalized System of Preferences, Decision of 25 June 1971, BISD18S/24, document L/3545, recital 1.

<sup>200</sup> Steve Charnovitz et al., *Internet Roundtable The Appellate Body’s GSP decision*, 3 *World Trade Review*, no. 2 (2004), 256.

<sup>201</sup> Gregory Shaffer and Yvonne Apea, *Institutional Choice in the Generalized System of Preferences Case: Who Decides the Conditions for Trade Preferences? The Law and Politics of Rights*, 39 *Journal of World Trade*, no. 6 (2005), 1001.

The EU GSP scheme contains 2 levels of preferences. The first one does not require the fulfilment of any conditions. The second one or the grant of additional preferences requires the fulfilment of these conditions which can be termed discriminatory. Therefore, the worst would be the withdrawal of the second level or additional preferences. Most potential beneficiaries are unable to fulfil these conditions and are thus unable to benefit from these additional preferences. In any case, the European Parliament has stated that the GSP utilisation rate needs to be improved.<sup>202</sup> Perhaps, the utilisation rate has not improved because beneficiaries are unable to fulfil conditions? So the GSP donors or the EU in this case could do away with conditions and grant more preferences at the first level itself. Moreover, the absence of conditions means that potential beneficiaries can benefit from their comparative advantage on which international trade is predicated. In fact, the European Parliament has stated that the GSP schemes, to improve their impact, should grant preferences in accordance with the comparative advantage of beneficiaries.<sup>203</sup> As a consequence, the benefits obtained through the GSP can be passed to least-developed countries since developing countries have agreed to provide preferences to them.<sup>204</sup>

The development of developed countries was not subject to such obstacles which have been made into law. Only the AB can interpret this law favourably for the developing countries. The fear of political reprisals in the form of withdrawal of GSP schemes should not prevent the AB from doing so. Much has been written on the subject and its political nature but the AB has the legal means to override the political issues involved and should have done so because such cases will not come for adjudication very frequently. The purpose of setting up the WTO was to reduce the power imbalance between countries but its purpose will be defeated if this imbalance exists within the Organization. Moreover, these issues cannot be resolved by 163 members due to lack of consensus but the AB only requires consensus between 2 of its members.

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<sup>202</sup> See paragraph E of P6\_TA(2004)0024 Generalised system of preferences European Parliament resolution on the Communication from the Commission to the Council, the European Parliament and the European Economic and Social Committee 'Developing countries, international trade and sustainable development: the function of the Community's generalised system of preferences (GSP) for the ten-year period from 2006 to 2015' (COM(2004)0461).

<sup>203</sup> See paragraph 6(a) of P6\_TA(2004)0024 Generalised system of preferences European Parliament resolution on the Communication from the Commission to the Council, the European Parliament and the European Economic and Social Committee 'Developing countries, international trade and sustainable development: the function of the Community's generalised system of preferences (GSP) for the ten-year period from 2006 to 2015' (COM(2004)0461).

<sup>204</sup> See Decision on Waiver Preferential Tariff Treatment for Least-Developed Countries adopted on 15 June 1999, WT/L/304, 17 June 1999 and Decision on Extension of Waiver Preferential Tariff Treatment for Least-Developed Countries adopted on 27 May 2009, WT/L/759, 29 May 2009.

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