The Legality of Conditional Preferences to Developing Countries under the GATT Enabling Clause

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An issue that has plagued the GATT/WTO system since its inception has been the question of how to handle the needs of both developed and developing countries in one coherent system. As developing countries make up approximately 75 percent of WTO membership,1 this is a very real concern for the future of the WTO. Accepting that developed countries have an obligation to support developing countries as they seek to develop, WTO members, in 1979, enacted the Decision on Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries (the “Enabling Clause”).2 The Enabling Clause suspends the GATT’s general most favored nation (“MFN”) rule and allows developed country members to give differential and more favorable treatment to developing countries. The mechanism for this treatment is the Generalized System of Preferences (“GSP”), under which developed countries offer non-reciprocal preferential treatment to products originating in developing countries. The GSP program is voluntary for developed countries, who also determine which countries receive preferences and to what extent those preferences are granted.

An ongoing question under the Enabling Clause has been the extent to which developed countries may condition the granting of a preference on the developing country’s attainment of certain non-trade-related goals. For example, developed countries have used this method of conditional preferences to tackle labor, environmental, and now, drug-related issues. In January 2003, after preliminary negotiations had broken down, the WTO Dispute Settlement Body granted a request from India for the Establishment of a Panel to address the European Communities’ (“EC”) Conditions for the Granting of Tariff

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Preferences to Developing Countries. India argued that two aspects of the EC scheme—conditions relating to drug production and trafficking and those relating to labor rights and the environment—are inconsistent with GATT and do not meet the requirements of the Enabling Clause. The Panel Decision in this case will be vitally important in shaping the future of the WTO. If the measure is allowed, the EC will be given a powerful tool for shaping the internal domestic policies of nations at crucial stages in their development; if it is prohibited, developing nations will be given a powerful freedom to achieve development on their own terms.

This Development will trace a short history of the Enabling Clause and the successes and failures associated with attempts to use the Clause to further other goals. It will then analyze the arguments put forth by India and the EC regarding the conditional preferences and will recommend that the Dispute Settlement Panel find in favor of India and reject the conditioning of GSP provisions on non-trade-related standards. Finally, this Development will address the possible future of the Enabling Clause as a mechanism for establishing developing country treatment of such goals as higher labor standards, environmental protection, and prevention of drug trafficking.

I. THE ENABLING CLAUSE

The Enabling Clause was instituted by the WTO in 1979 to address the role of developed countries in the economic progress of developing countries. The Decision provides that “contracting parties may accord differential and more favourable treatment to developing countries, without according such treatment to other contracting parties.” The Clause allows developed member nations to apply “[p]referential tariff treatment . . . to products originating in developing countries in accordance with the Generalized System of Preferences.” This approach was designed to promote flexible commitments for developing countries and to encourage developed countries to broaden market access to those countries. The Uruguay Round Agreements and subsequent


4 Enabling Clause ¶ 1 (cited in note 2).

5 Enabling Clause ¶ 2(a) (cited in note 2).
WTO Declarations include nearly 150 provisions concerning special and differential treatment.\(^6\)

In practice, the Enabling Clause has proved to be a continuing source of confusion among WTO Members.\(^7\) Contrary to the GATT’s general MFN obligation, the Decision’s language is thought not to require that once a developed nation extends preferential tariff treatment to one developing nation, it then extends such preferential treatment to all developing nations. Likewise, the extension of preferential treatment is voluntary and may be revoked by the developed country at any time.\(^8\) A more complicated question is whether developed countries can condition the receipt of preferential tariff treatment on a developing country’s meeting certain non-trade goals.

II. TO WHAT EXTENT CAN THE ENABLING CLAUSE BE USED TO BROADEN THE WTO’S AGENDA?

Developed countries argue that the Enabling Clause permits them to condition the promise of additional preferential market access on the domestic standards of the developing country. According to this conception, the GSP system would allow a developed country to do something that it could not legally do under the general GATT provisions. For example, in the labor standards context, under the GATT/WTO system, a member nation could not prohibit the importation of a certain good or goods from a nation with lower labor standards, nor could the country apply heavier tariffs to such goods.\(^9\) Such actions would violate GATT Articles XI and II, respectively, and would not be cured by the exceptions in Article XX as they could be challenged as “disguised restriction[s] on international trade.”\(^10\) Proponents of conditional preferences argue that the special nature of the preferential GSP scheme does allow for such conditionality as would otherwise be prohibited by GATT.

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\(^{9}\) See, for example, Belgian Family Allowances (*Allocations Familiales*): Report Adopted by the Contracting Parties on 7 November 1952 (G/32), 1 GATT BISD 60 (1953). In this early case, the WTO Panel considered a Belgian policy under which a levy was applied on imports purchased by governmental entities where the country of origin was determined to have a less progressive system of family allowances than did Belgium. The Panel concluded that the “social policy considerations” were “irrelevant” to their determination of whether the levy violated the requirement that like products be treated equally.

\(^{10}\) General Agreement on Tariffs and Trade art XX, 1 GATT BISD 10 (1952), 55 UN Treaty Ser 262 (1950).
The Enabling Clause has most commonly been used to link GSP commitments to labor standards. For example, in 1998, the EC amended its GSP to include "special incentive arrangements for the protection of certain labor rights." Developing countries that already receive preferential duties applied to their exports to the EC may request more preferential rates only if they agree to abide by the International Labor Organization Conventions concerning the rights to organize and to bargain collectively and the minimum age for employment. Such developing countries must also submit to a rigorous control procedure by the EC. Likewise, the US has enacted national legislation to provide for the granting of duty-free benefits to developing countries, contingent upon the satisfaction of certain criteria. For example, the Trade Act of 1974 instructs the President to take into account "whether or not such country has taken or is taking steps to afford to workers in that country . . . internationally recognized worker rights" when determining whether to name a country a beneficiary developing country.

The GSP system allows granting countries enormous discretion in both the scope and design of preferences. Because the extension of preferential treatment is voluntary and entirely within the discretion of the donor country, such commitments depend largely on political considerations. Developing countries have thus far refrained from challenging the GSP schemes either for lack of consistency (similar countries receiving differing treatment) or for conditions placed upon such treatment. It has been suggested that developing countries refrain from posing such challenges because "they would rather be on good terms with GSP donors." Developing countries that receive preferences want to retain them, and developing countries that do not receive such preferences are fearful of jeopardizing their chances of receiving them in the future.

The Dispute Settlement Body was nearly given the opportunity to consider these issues in 2000, when Brazil requested consultations with the EC regarding EC practices that Brazil claimed were inconsistent with the Enabling Clause. However, Brazil did not follow up by requesting the establishment of a panel. Commentators speculate that it was political pressure that caused this move on
Brazil’s part. Therefore, the pending dispute between the EC and India will be the Dispute Settlement Body’s first opportunity to address these issues.

III. THE EC–INDIA DISPUTE

In June 2001, the European Commission adopted a new scheme of tariff preferences for developing countries. Upon the adoption, Pascal Lamy, Trade Commissioner for the European Union, called the scheme “the most generous GSP package ever put forward by the European Union” and noted that the scheme provided “further concrete evidence that the interests of developing countries are at the top of [its] agenda.” Under the package, the “special incentive arrangements for the protection of labour rights and of the environment become significantly more attractive.” Under the EC GSP currently in place, developing countries that qualify for “special incentive arrangements” relating to protection of labor rights and the environment and to the “drug regime” may be granted reduced tariff rates or have their tariff obligations suspended.

India is a beneficiary country under the EC’s scheme of generalized tariff preferences. Under the EC’s GSP scheme for 2002–2004, several of India’s tariff preferences were removed. India is not included in the EC’s special arrangements to combat drug protection and trafficking, for the protection of labor rights, or for the protection of the environment.

In December 2002, India requested the establishment of a Panel to investigate the legality of the EC regime under the WTO. India is particularly

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20 Id at 2.
22 Id at 32.
23 World Trade Organization, European Communities—Conditions for the Granting of Tariff Preferences to Developing Countries (cited in note 3). Other developing countries, including Colombia and Venezuela, requested to participate in the initial consultations in light of their substantial interests. See World Trade Organization, Request to Join Consultations, Communication from Colombia, European Communities—Conditions for the Granting of Tariff Preferences to Developing Countries, WTO Doc No WT/DS246/3 (Apr 5, 2002), available online at <http://www.wto.org/english/tratop_e/dispu_e/dispu_status_e.htm> (visited Sept 7, 2003); World Trade Organization, Request to Join Consultations, Communication from
concerned about two aspects of the EC’s GSP scheme. First, the tariff preferences accorded for combating drug production and trafficking are available only to certain countries selected by the EC. Second, the preferences available under the special incentive arrangements for the protection of labor rights and the environment are accorded only to countries that meet labor and environmental policy standards determined by the EC. India believes that the tariff preferences granted under these special arrangements create undue difficulties for India’s exports and nullify or impair the benefits accruing to India under the MFN provisions. India argued that preferential treatment is an exception to a developed nation’s MFN obligations only so far as it allows discrimination in favor of developing countries. India further argued that the exception was intended solely “to facilitate and promote the trade of developing countries.”

The EC responded to India’s allegation by claiming that the GSP scheme is an “autonomous regime granted on a non-reciprocal, generalized and non-discriminatory basis, in full conformity with the EC’s GATT/WTO commitments, including the Enabling Clause.” The EC maintains that the special incentives are designed to further internationally recognized objectives and to promote sustainable development.

As noted previously, this will be an issue of first impression for the Dispute Settlement Body (“DSB”). Its resolution will carry significant consequences as to the proper scope of the WTO as it seeks to rise to the challenge posed by the integration of developing countries into the WTO framework. This analysis will now turn to the legal arguments available to the parties and to the policy considerations that the Panel will be required to take into account. Finally, the analysis will seek to recommend an outcome of the dispute and comment on its suitability.
A. Arguments Available to Developing Countries

India’s strongest argument may well come from the text of the Enabling Clause itself. Importantly, the Clause states that “[a]ny differential and more favourable treatment . . . shall be designed to facilitate and promote the trade of developing countries and not to raise barriers to or create undue difficulties for the trade of any other contracting parties” and “shall . . . respond positively to the development, financial and trade needs of developing countries.”29 GSP preferential arrangements should, therefore, aim to facilitate trade, should not create obstacles to the trade of third countries, and should not impede MFN-based liberalization. The Enabling Clause also states that the measures enacted under the auspices of the GSP “should promote the basic objectives of [GATT].”30 These requirements suggest that all preferences granted under the Clause must be directly related to beneficial trade consequences.

These provisions underscore the general concern for the promotion of developing countries that is evident within the WTO system. The GSP is intended to compensate for the relative disadvantages of developing countries in the competitive global marketplace and “to facilitate their industrialization [sic].”31 For decades, the WTO has made clear that one of the Contracting Parties’ primary goals is the increased inclusion of less-developed countries in world markets and improved market access.32 Indeed, GATT Part IV specifically tackles the particular challenges that developing countries face.33

The importance of this general theme is pivotal for India because it underscores the fact that the purpose of the GSP is to aid developing countries and suggests that conditions that are unrelated to that goal, or worse yet that are contrary to it, should not be permitted. For example, developing nations included in the EC’s special arrangements for the protection of the environment may be granted a preference conditioned on that nation’s attainment of certain environmental standards (potentially unrelated to trade arrangements). Although the GSP is fundamentally voluntary on the part of developed nations, India could reasonably argue that the stated purpose of the Enabling Clause is to aid developing countries and that goal should not be eclipsed by other unstated goals, such as environmental protection.

It is also beneficial for India that DSB Panel decisions demonstrate a general reluctance to impose one country’s standards upon another. Two general

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29 Enabling Clause ¶ 3, 3(a), (c) (cited in note 2).
30 Id ¶ 7.
33 Id.
principles established by the *Tuna-Dolphin* Panel are significant here. First, where there is no direct impact on the importing nation, the exporting nation is given sole discretion over its production processes. Second, trade restrictions governing production process decisions are best enacted through multilateral agreements. These underlying principles suggest that the imposition of such standards has no place in the WTO system, at least not in its current form.

As noted previously, in its Request for the Establishment of a Panel, India expressed concern that the EC GSP system affords preferences only to certain developing nations chosen by the EC. Although the text of the Enabling Clause does not make it particularly clear whether such discrimination between developing countries is allowed, as noted previously, the language is generally thought not to require that preferential treatment be extended to all developing countries once it is extended to one. Therefore, it seems likely that India may lose on this point. India may be wise to focus instead on the issues raised in the previous paragraphs in this Part. That is not to say, however, that the argument could not be shaped so as to afford India the protection from unequal treatment it is ultimately seeking.

**B. ARGUMENTS AVAILABLE TO DEVELOPED COUNTRIES**

The European Community may be most successful by focusing its argument on the inherently different nature of the GSP system as compared to the general provisions of trade law under GATT. The GSP allows the general GATT rules to be suspended in favor of developing countries so as to encourage their progress. It is arguable that by suspending the prohibition on tariff rates conditional on exporting country conditions, the GSP could go even further toward aiding developing countries in achieving development.

For example, the EC could argue that although the GSP bias in favor of developing countries would not be sustainable under GATT (for the reasons stated previously), the GSP is a special system designed to alleviate the otherwise heavy burden on developing countries. It is undisputed that the general financial aid given by one country to another may be conditioned upon whatever requirements the donor country sees fit. It would follow, therefore, that because the preferential system is a voluntary one granted by developed countries at their discretion, the granting of the preferences carries with it the ability to qualify the preference as the developed country sees fit.

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35 See Enabling Clause ¶ 1 (cited in note 2) ("[C]ontracting parties may accord differential and more favourable treatment to developing countries, without according such treatment to other contracting parties.") (emphasis added).
The question of whether drug trafficking and environmental protection provisions may be made conditions of a developing country’s receiving preferential tariff rates has not been addressed in either the courts or (to a significant extent) in the literature. However, conditioning treatment on labor standards is both fairly common among developed countries and fairly well analyzed in the literature. “The imposition of a labor condition appears not to offend GATT obligations since a waiver of the basic MFN obligation enables the operation of the Generalized System of Preferences.” The EC would, therefore, do well to contend that the other two conditions imposed by the EC regulation—drug prevention and environmental protection—are the functional equivalents of labor standards and should thus be treated similarly. This argument is plausible because in a broad sense each of these standards furthers a common goal. The developed country imposing the standard is basically saying, “you are allowing something that we do not approve of (environmental degradation, trafficking in illegal drugs, child labor, or unsafe labor conditions) and as a result we believe that our country is being harmed (either directly or in some larger sense). Therefore, we will give you preferential trade treatment but only on the condition that you stop allowing these negative things.” In such a broad sense, these conditions do seem sufficiently similar.

The EC should note, however, at least two significant counterarguments to that classification. First, a strong argument could be made that labor standards and drug trafficking/environmental protection are not similar enough to justify the connection. Labor standards are much more closely tied to trade in goods than are drug trafficking provisions, and to a lesser extent, environmental protection. Perhaps if one concludes that GSP schemes are not the proper mechanism through which to tackle labor standards, then one would conclude even more vehemently that drug trafficking is certainly not properly addressed in that context, as the connection between drugs and trade in other goods is even more tenuous. Second, although many commentators believe that imposing labor conditions under the GSP does not violate GATT, that is certainly not a foregone conclusion and there is reasonable disagreement on that point. Further, even if plausible under GATT, there is contention over whether imposing conditional preferences is the right way to encourage development. The US legislation has attracted particular attention. The establishment of an internationally imposed labor standard by the US “has been decried by some as aggressive unilateralism and welcomed by others as a fitting way to link economic and social progress.”

37 Id.
In general, the EC should push for a slightly broader conception of the purpose of the WTO. Surely the WTO exists to promote fair trade, but at least in the context of the GSP, it also exists to promote growth and sustainable development in developing countries. One of the ways that it does so is through financial support by developed countries and the encouragement of improved standards of living, which arguably is what the EC is trying to accomplish here.

C. RESOLUTION AND RECOMMENDATIONS

Both India and the EC have strong arguments in their favor, and the governing treaty provisions and WTO decisions are vague enough to allow the Panel to decide in either party’s favor. However, I believe that the Panel should resolve this dispute in favor of India and the developing nations. Such a decision is necessary to maintain the character of the GSP as a structure to foster the incorporation of developing countries into the global economy.

Allowing conditional preferences would mean that developed countries could structure the GSP imposed on developing countries according to their own desires and political ambitions. The granting of such preferences is clearly in conflict with the goals of the Enabling Clause to promote trade of developing countries without raising barriers or creating undue difficulties. Allowing freedom in structuring preferences in this way could impose conditions on developing nations that far outweigh the benefits that they would receive from the preferential tariff. Such a system runs the danger of becoming a means for developed nations not only to impose their values on other countries but also to restrict those nations from developing at all. For example, the EC’s rigorous control and monitoring procedure alone could make participation in the GSP system prohibitively difficult for many countries. Such procedures defeat the purpose of the preferential system.

Allowing such conditional preferences would open the door for those who believe that developed countries should be permitted to condition their GSP schemes to call for additional and even less appropriate conditions. For example, some commentators argue that “curbing transnational bribery should become a WTO goal.” If the Panel were to decide in favor of the EC, it could be argued that the decision serves as precedent for a scheme that conditions the granting of preferences on the nation’s having in place measures to combat transnational bribery. Such a decision could mean that any interest group with a modicum of political clout could persuade developed nations to condition trade preferences on developing countries’ advancements towards their specific goal. There are an infinite number of challenges facing the global community. Developing countries already argue that standards imposed by developed nations are too...

imposing, and thus, prevent them from actively participating in the global marketplace. Allowing additional conditional preferences causes a significant risk of ensuring that developing countries will never be permitted to become active partners in the international economy.

Finally, as noted previously, few would disagree with the contention that financial aid granted by one country to another may be conditioned upon whatever requirements the donor country sees fit. However, the tariff preferences system is not properly considered aid in the same sense. As such preferences are part of a larger trade network, there is not necessarily room for developed countries to impose their national standards on less-developed countries as a condition for their receipt of those preferences. Should the Panel allow such conditional preferences, the character of the WTO would change definitively and significantly. While certainly possible, such a transformation is properly accomplished not unilaterally, but through a comprehensive new WTO agreement.

IV. Conclusion

The decision will come down to a fundamental choice about the mission of the WTO in the next century—is the WTO to be a regulating body ensuring fair trade between diverse nations, or a global organization with a broad agenda, including labor, environmental, and drug trafficking goals? Jose Alvarez and Steve Charnovitz argue that “one of the biggest challenges” currently facing the WTO is “to determine its own mission.” There is ongoing dispute over the extent to which the WTO framework should be expanded to include room for other issues of international concern, particularly higher labor standards and environmental protection. The debate is active even within the leadership of the WTO. In early 2001, former Directors General of the GATT or the WTO, Arthur Dunkel, Peter D. Sutherland, and Renato Ruggiero, circulated a public statement expressing their opinion that “[t]he WTO [should not] be used as a Christmas tree on which to hang any and every good cause that might be secured by exercising trade power.” However, later that year, acting WTO Director-General Mike Moore responded that governments “urgently need to broaden the agenda beyond the mandated negotiations” included in the WTO agreements. In the upcoming Dispute Settlement, the Panel has the opportunity to alter the character of the WTO. However, such a transformation would be inappropriately positioned there. If developed countries are concerned about labor standards, environmental protection, or drug trafficking, there are

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39 Id at 28.
40 Id.
41 Id.
other avenues open to them in which the propagation of international standards should be sought.