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# Power and Preferences: Developing Countries and the Role of the WTO Appellate Body

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# Power and Preferences: Developing Countries and the Role of the WTO Appellate Body

## **Cover Page Footnote**

International Law; Commercial Law; Law

# **Power and Preferences: Developing Countries and the Role of the WTO Appellate Body**

*Peter M. Gerhart<sup>†</sup> & Archana Seema Kella<sup>††</sup>*

## **ABSTRACT**

Although it is conventional to view the World Trade Organization (WTO) as a law-based regime, we should not underestimate the ways in which state power has molded, and continues to mold, the regime. Understanding the role of power is especially important for our understanding of the relationship between developed and developing countries, the disparity of power between the two has provided the GATT/WTO regime with the challenge of trying to incorporate the powerless developing states into a system that is built on power. We review that challenge in the context of the dispute over the conditions that developed countries impose when they give developing countries preferential trade agreements. Because such preferences are, in theory, gifts, not exchanges, they should be understood as methods by which powerful countries recognize and respond to the powerlessness of the developing countries. Yet as developed countries put more and more conditions on the preferences, they diminish the redistributive character of the preferences, and the preferences begin to look like additional sources of power rather than unilateral gifts to powerless states.

We examine the role of the WTO's Appellate Body in monitoring this dynamic between the powerful and powerless states. Although the Appellate Body performs a judicial, interpretive function, its role in the WTO calls for a far more politically sensitive posture. Without abandoning its interpretive function, the Appellate Body must be attentive to the systemic values that drive the WTO regime. We believe that within the interpretive discretion that it has, the Appellate Body has

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recognized, and should exercise, the role of monitoring the power relationships between developed and developing countries.

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### I. Introduction

Our tendency, when confronted with a new institution, is to try to understand and appraise it by drawing analogies to institutions that are familiar to us. Therefore, when the World Trade Organization (WTO) was founded a decade ago, its dispute settlement system was thought to be similar to the judicial branch of any governing organization – independent from the “lawmaking” branch by serving only an adjunct, interpretive function.<sup>1</sup> As apt as the analogy is, even judicial bodies take their character from their surroundings, and this has proven to be true of the “judicial branch” of the WTO – the Panels and, especially, the Appellate Body that oversee the dispute settlement system.<sup>2</sup> Over

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<sup>1</sup> See generally Peter M. Gerhart, *The Two Constitutional Visions of the World Trade Organization*, 24 U. PA. J. INT’L ECON. L. 1 (2003) (showing that the WTO can best be understood as an institution of international participatory lawmaking, giving each member an opportunity to participate in the lawmaking of other members).

<sup>2</sup> The “judicial” branch of the WTO was created under the Understanding on Rules and Procedures Governing the Settlement of Disputes, commonly referred to as

the past ten years, it has become apparent that the Appellate Body plays a unique judicial role in the WTO multilateral trade regime.<sup>3</sup> This article argues that the Appellate Body must, in the context of its interpretive function, modulate the power relationships between developed and developing countries in order to uphold the systemic values underlying the WTO regime.

The Appellate Body's 2004 decision in *European Communities—Conditions for the Granting of Tariff Preferences to Developing Countries* (hereinafter *EC-Conditional Preferences*)<sup>4</sup> provides a lens to assess the role of the Appellate Body with respect to the power relationships among WTO members. Although the decision, on its face, appears to be quite narrow, its implications for understanding the WTO are quite broad. In particular, the decision allows us to examine anew both the role of developing countries in the WTO system and the judicial role of the Appellate Body in interpreting the treaty obligations of WTO members.

The *EC- Conditional Preferences* case was brought by India to challenge preferences in the form of lower tariffs that the European Communities (EC) made available to Pakistan but not to India.<sup>5</sup> The EC's preference program designated Pakistan as an eligible beneficiary country because of its drug trafficking and

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the Dispute Settlement Understanding (DSU), which authorizes the Dispute Settlement Body (DSB) to establish panels, adopt Panel and Appellate Body reports, maintain surveillance of how countries implement rulings and recommendations, and authorize suspension of concessions and other obligations under the covered agreements. WTO, *Understanding on Rules and Procedures Governing the Settlement of Disputes*, available at [http://www.wto.org/english/tratop\\_e/dispu\\_e/dsu\\_e.htm](http://www.wto.org/english/tratop_e/dispu_e/dsu_e.htm) (last visited Feb. 21, 2005) [hereinafter WTO, *Understanding on Rules and Procedures*]. Unlike the dispute system under GATT, the DSU provides strict timelines on proceedings, the right to a Panel, review by the Appellate Body, and automatic adoption of reports. Marc L. Busch & Eric Reinhardt, *Developing Countries and General Agreement on Tariffs and Trade/World Trade Organization Dispute Settlement*, 37 J. WORLD TRADE 719, 721 (2003).

<sup>3</sup> For a comprehensive review of the similarities and dissimilarities between dispute settlement at the WTO and domestic dispute resolution, as well as an appraisal of dispute settlement in the context of the evolving international trade regime, see Donald McRae, *What is the Future of WTO Dispute Settlement?*, 7 J. INT'L ECON. L. 3 (2004).

<sup>4</sup> *European Communities – Conditions for the Granting of Tariff Preferences to Developing Countries*, REPORT OF THE APPELLATE BODY, WT/DS246/AB/ R (Apr. 7, 2004), available at [http://www.wto.org/english/tratop\\_e/dispu\\_e/246abr\\_e.doc](http://www.wto.org/english/tratop_e/dispu_e/246abr_e.doc) (last visited Feb. 21, 2005) [hereinafter AB REPORT].

<sup>5</sup> See *Id.*

production reduction programs.<sup>6</sup> India, however, was not designated as an eligible beneficiary country. Because Pakistan's producers faced lower European tariffs than Indian producers, some Pakistani producers had more favorable access to European markets than producers from India.<sup>7</sup>

The narrow issue in the case, therefore, was whether, and to what extent, a developed country may discriminate between similarly situated developing countries when designing a program under the Generalized System of Preferences (GSP) system.<sup>8</sup> As is described in greater detail later,<sup>9</sup> the Appellate Body ruled that a developed country granting lower tariffs under the GSP Program need not treat all recipient countries alike, but that any differential treatment of developing countries must be based on positive, objective criteria that, when fairly applied, distinguish between developing countries on a basis that reflects their different developmental needs.<sup>10</sup> Based on these positive and objective development criteria, all similarly situated countries must be treated alike.<sup>11</sup> In so ruling, the Appellate Body not only clarified the legal framework for assessing conditional and differential treatment, but also provided a picture of the logic underlying the GSP program and the role of developing countries in the WTO system.

The scholarly commentary on the issues raised in *EC—Conditional Preferences* has been mixed, reflecting preexisting views about the relationship between developed and developing countries. Some scholars contend that GSP programs should not be subject to “hard law” constraints that unduly bind the freedom of developed countries to determine the basis on which they will

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<sup>6</sup> See *infra* notes 145-72 and accompanying text.

<sup>7</sup> Because the preferences were discriminatory, they created artificial advantages for Pakistani producers, and it is possible that Pakistani producers made sales in Europe that could have been made more efficiently by producers in India; thus, the discrimination had the political and economic impacts of any preferential trading agreement. See BELA BALASSA, *THE THEORY OF ECONOMIC INTEGRATION* (1961); *THE ECONOMICS OF INTEGRATION*, M. KRAUSS (ed.) (1973); A. EL-ALGRAA & A. JONES, *THEORY OF CUSTOMS UNIONS* (1981).

<sup>8</sup> See AB REPORT, *supra* note 4.

<sup>9</sup> See *infra* notes 143-72 and accompanying text.

<sup>10</sup> *Id.*

<sup>11</sup> See AB REPORT, *supra* note 4.

provide preferences.<sup>12</sup> Under this view, the Appellate Body has only a narrow role in reviewing the conditions that donor countries place on their preferences, and controversies surrounding these conditions must instead be addressed in political negotiations.<sup>13</sup> This view emphasizes the importance of maintaining the ability of a donor country, such as the United States, to grant or withdraw GSP treatment based on its own policy objectives and political values.<sup>14</sup> Other commentators, however, are not particularly troubled by the notion that the Appellate Body could have a role in reviewing the terms under which preferences are granted.<sup>15</sup> Still other scholars are sympathetic to the plight of developing countries, and have been highly critical of the conditions that donor countries have attached to the preferences they give.<sup>16</sup> Commentary appearing since the Appellate Body opinion issued the *EC Conditional Preferences* decision has questioned aspects of the Appellate Body's opinion without trying to evaluate its impact on the multilateral trading system.<sup>17</sup>

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<sup>12</sup> See generally 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 CHI. J. INT'L L. 385 (2003) (arguing that GSP is aspirational only and therefore not subject to judicial control) [hereinafter Howse, *India's WTO Challenge*]; Robert Howse et al., in *Internet Roundtable, The Appellate Body's GSP Decision*, 3 WORLD TRADE REVIEW 239, 246 (2004) [hereinafter *Internet Roundtable*]; 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 Preference*, 18 AM. U. INT'L L. REV. 1333 (2003) (analyzing India's additional preferences for countries that meet labor and environmental standards) [hereinafter *Back to Court After Shrimp/Turtle*].

<sup>13</sup> See Howse, *India's WTO Challenge*, *supra* note 12.

<sup>14</sup> See *id.* at 386.

<sup>15</sup> See generally Lorand Bartels, *The WTO Enabling Clause and Positive Conditionality in the European GSP Program*, 6 J. OF INT'L ECON. L. 507 (2003) (assessing the system of positive conditionality in light of WTO rules); Gregory Shaffer & Yvonne Apea, *Putting the GSP Case in Context: Who Decides the Conditions for Trade Preferences*, in *TRADE AND HUMAN RIGHTS* (Thomas Cottier & Joost Pauwelyn, eds., 2005) (publication forthcoming) (outlining the institutional choices that the Appellate Body faced when deciding the case).

<sup>16</sup> See generally Abdulqawi A. Yusuf, "Differential and More Favorable Treatment:" *The GATT Enabling Clause*, 14 J. WORLD TRADE L. 488 (1980) (reviewing development of the GSP as a benefit to developing countries).

<sup>17</sup> See generally Howse et al., *Internet Roundtable*, *supra* note 12, at 239 (finding benefit in Appellate Body reversal and seemingly supporting Appellate Body

Our view of the opinion draws on many of these ideas, but because we see the Appellate Body's opinion<sup>18</sup> as more far-reaching than the narrow holding would suggest, we evaluate the opinion in a wider context. Because the decision focused on the purpose of the GSP program in the context of the relationship between developed and developing countries,<sup>19</sup> the Appellate Body's holding necessarily implicates questions about the role of power in the WTO regime. Not only does the Appellate Body's opinion suggest how we may understand conditions that granting countries place on their GSP programs – a matter of great contention between developed and developing countries – but it also forces us to examine the role that power plays in the WTO system, and the role that the Appellate Body plays with respect to the power relationships. In particular, the Appellate Body's opinion gives us occasion to think about the GSP program in political, rather than legal, terms and to understand in new ways the role of the Appellate Body as an intermediary power broker between strong and weak WTO member notions.

Because our interpretation of the Appellate Body's role hinges on the nature of power within the WTO system, we direct our attention to that issue first. Part II of this article discusses the role and nature of power within the General Agreement on Tariffs and Trade (GATT) and WTO system, and the role that the GSP program has played to integrate countries with little economic power into this system. Our portrayal of the role of developing countries differs from traditional accounts because we emphasize the political, rather than economic, factors that influence the position of developing countries. By viewing the GSP programs as antidotes to the relative powerlessness of developing countries, we situate the legal issue before the Appellate Body in political, rather than legal, terms. To be sure, a legal standard governs the conditions that a donor country may impose, but the political reality shows that the underlying problem addressed by the GSP system is one of power. This political orientation exposes the

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endorsement of multilateral agreements as creating WTO-relevant norms), and Howse et al., *Internet Roundtable*, *supra* note 12, at 241 & 245 (noting the "important practical implications for conditionality on the EC and US GSP programs").

<sup>18</sup> AB REPORT, *supra* note 4.

<sup>19</sup> *Id.*



underlying dilemma in the legal oversight of GSP programs: preferences are given at the discretion of developed countries, not pursuant to obligations required by the treaties or the WTO. The voluntary nature of preferences has induced developed countries to grant preferences conditionally. It is the nature of those conditions that is at the heart of legal and political disputes about the administration of GSP programs.

To explore conditional preferences under the GSP system in a larger context, however, we note that conditional GSP preferences are not an isolated phenomenon. They are similar in nature to any gift that carries with it conditions. Part III of this Article therefore provides an analytical framework for understanding the general legal attitude toward conditional gifts -and the circumstances under which conditional gifts can become tools of impermissible power. This Part addresses the general claim that because gifts do not have to be given, adding conditions to the gifts cannot be objectionable. Here, we rely on theories of unconstitutional conditions and gifts against public policy to show the circumstances under which gifts or privileges may not be conditioned on the recipient surrendering certain rights or freedoms.

Part IV then summarizes the decision of the Appellate Body in the *EC-Conditional Preferences* case, showing how the Appellate Body interpreted the relevant law to reflect conditionality limits that are inherent in the WTO scheme for preferences.<sup>20</sup> Here, we emphasize the Appellate Body's understanding that GSP privileges must be administered with an awareness of the recipient country's powerlessness.

Next, in Part V of the article, we extrapolate from the Appellate Body's holding to articulate a general framework for analyzing the conditions that granting countries place on GSP programs. This provides the reader with a set of general principles that are likely to determine the outcome of future challenges to conditional GSP programs.

Our concern, however, is not just the legal, but also the political, ramifications of the decision in *EC-Conditional Preferences*. We discuss those political ramifications in Section VI, explaining how the Appellate Body, through this ruling, has

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<sup>20</sup> AB REPORT, *supra* note 4.

placed itself in a position to oversee the power relationships among members in the WTO system. This position enables the Appellate Body to place meaningful limits on the exercise of power by the developed countries, while also recognizing that power cannot be avoided in a system of law that is based on bargaining power. Thus, we identify a role for the Appellate Body that has heretofore gone unnoticed; a role in which the Appellate Body's interpretive function must be undertaken with a view toward the systemic interests that lie at the heart of the WTO system. We recognize the Appellate Body as a systemic stabilizer that is able to tilt its interpretations in a way that provides all the disparate members of the WTO with good reasons to continue their support of the GATT/WTO system.

Part VII concludes with a summary of our analysis and explains why the political, systemic function that we identify for the Appellate Body is an appropriate basis for its exercise of judicial power.

## II. Power in the WTO

Integrating developing countries into the GATT/ WTO regime has been a complicated process.<sup>21</sup> Although most scholars contend that the reason for the uneasy integration is that the developing countries have a different relationship to free trade than developed countries, as we explain in this section, that rationale is an incomplete understanding of the issue.<sup>22</sup> The position of developing countries in the WTO is as much a reflection of their lack of power as it is a reflection of their economic interests or integrating capacities.<sup>23</sup> Relative power remains an integral feature of the WTO regime.<sup>24</sup> Even though the WTO now oversees as rule-based system, and even though the legal obligations of such a law-based, rule-oriented system can be costly to ignore, it must be understood that the basis on which that law is made is power, not democratic decision making.<sup>25</sup>

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<sup>21</sup> Richard H. Steinberg, *In the Shadow of Law or Power? Consensus-Based Bargaining and Outcomes in the GATT/WTO*, 56 INT'L. ORG. 339, 341-47 (2002).

<sup>22</sup> *Id.*

<sup>23</sup> *Id.*

<sup>24</sup> *Id.*

<sup>25</sup> *Id.*

### A. *The Role of Economic Power*

The WTO's primary purpose is to allow members to bargain with each other in order to obtain binding commitments to change policies that adversely affect the welfare of other member countries.<sup>26</sup> This bargaining is inherently power-based.<sup>27</sup> WTO members negotiate market access commitments, for example, based on the size and diversity of their economies.<sup>28</sup> Members with the greatest economic wealth and most diversified economies, such as the United States and the EC, have more to offer in negotiations and less to lose in the event that negotiations break down.<sup>29</sup> Thus, they have more bargaining power than other members. At the other end of the spectrum, members with little wealth and diversity in their economies have the least to offer in any given negotiation and the most to lose if the negotiations are unsuccessful.<sup>30</sup> Consequently, in the absence of effective coalition building or other strategic considerations, these countries have the least bargaining power in the system and wealthy countries are significantly more likely to secure their desired outcomes under the WTO.

Over the years the GATT/WTO system has become increasingly subject to legal, rather than political, control.<sup>31</sup> As members have taken on new commitments, the power of the wealthy countries has been decreased, and some commitments

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<sup>26</sup> Gerhart, *supra* note 1.

<sup>27</sup> Steinberg, *supra* note 21 (conceptualizing the two modalities of bargaining power as law-based and power-based and finding that when trade rounds are law-based, more equitable results have been achieved but when trade rounds are power-based, asymmetrical contracts favoring the interests of powerful states are more likely). See also Gregory Shaffer, *Power, Governance and the WTO: A Comparative Institutional Approach*, in *POWER AND GLOBAL GOVERNANCE* (Michael Barnett & Raymond Duvall, eds. 2004).

<sup>28</sup> Steinberg, *supra* note 21.

<sup>29</sup> While it is difficult to accurately measure power, relative market size offers the best approximation of bargaining power in trade negotiations, with governments treating foreign market opening and associated increases in export opportunities as a domestic political benefit and domestic market opening as a cost. *Id.* Consequently, market opening and closure are treated as the currency of trade negotiations. *Id.*

<sup>30</sup> *Id.*

<sup>31</sup> See generally JOHN H. JACKSON, *THE WORLD TRADING SYSTEM* 109-111 (2d ed. 1997) (comparing the new rule based system of the WTO after the Uruguay Round with the prior power-oriented system of GATT).

have been directly aimed at reducing the use of unilateral power by the wealthy countries.<sup>32</sup> Moreover, the new dispute resolution architecture allows each member to hold other members accountable for their commitments; this form of legalization has replaced the negotiated settlement of disputes (which is inherently power-based) with the level playing field of judicial review.<sup>33</sup>

We should not, however, jump too quickly to the conclusion that in today's regime the relative power of countries is unimportant. Clearly, as WTO members undertake negotiations to work out the implementation of the GATS agreement<sup>34</sup> or in the new Doha Round of multilateral negotiations,<sup>35</sup> member's relative power continues to be an important force in determining the nature of the obligations that are undertaken and avoided. In these negotiations, the relative power of the members continues to shape the negotiations, both in process and in outcome.<sup>36</sup> If nothing else,

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<sup>32</sup> One of the achievements of the Uruguay Round of negotiations that ended in 1994 was a set of treaty provisions that were designed to limit the use of power to influence commitments made in negotiations, whether in the context of dispute resolution or in general negotiations. See generally WTO, *Understanding on Rules and Procedures*, *supra* note 2 (seeking, via Article 23, to channel disputes between countries concerning the obligations in the WTO treaties into the dispute settlement procedure); WTO, *Agreement on Safeguards*, available at [http://www.wto.org/english/docs\\_e/legal\\_e/25-safeg.doc](http://www.wto.org/english/docs_e/legal_e/25-safeg.doc) (last visited Feb. 21, 2005) (prohibiting, through Article 11, the use of unilateral action to seek voluntary restraints on trade between member countries).

<sup>33</sup> WTO, *Understanding on Rules and Procedures*, *supra* note 2.

<sup>34</sup> GATS, the General Agreement on Trade in Services, was completed as part of the Uruguay Round agreements, but its implementation called for, and has led to, additional negotiations for various service sectors. See, e.g., [http://www.wto.org/english/tratop\\_e/serv\\_e/serv\\_e.htm](http://www.wto.org/english/tratop_e/serv_e/serv_e.htm) (last visited Feb. 21, 2005). See OECD, *GATS: THE CASE FOR OPEN SERVICE MARKETS* (2002), available at <http://www.oecd.org/dataoecd/50/50/2088515.pdf> (last visited Feb. 21, 2005); OECD, *QUANTIFYING THE BENEFITS OF LIBERALIZING TRADE IN SERVICES* (2003) available at <http://www.www1.oecd.org/publications/e-book/2203011E.pdf> (last visited Feb. 21, 2005). For commentary on the defects in the negotiations over trade in services, see Bernard Hoekman, *Toward A More Balanced and Comprehensive Services Agreement*, in JEFFREY J. SCHOTT, *THE WTO AFTER SEATTLE*, 119 (2000) (reviewing difficulty of achieving balanced concessions in services negotiations).

<sup>35</sup> The Doha Round is the name given to the current round of multilateral negotiations begun at the Ministerial Conference in Doha, Qatar. Developments during the round are reported by the WTO at [http://www.wto.org/english/tratop\\_e/dda\\_e/dda\\_e.htm](http://www.wto.org/english/tratop_e/dda_e/dda_e.htm) (last visited Feb. 21, 2005).

<sup>36</sup> Thus, considerable attention is given to how the developing countries will be involved in the negotiations in order to avoid prior procedural problems. See generally SCHOTT, *supra* note 34, at 283 (discussing developing country dissatisfaction with

the search for ways to put together bargaining coalitions, and the counter-efforts to break up coalitions, shows that power remains the central ingredient of lawmaking by negotiation.<sup>37</sup> Moreover, despite the efforts noted above, the WTO system has proven to be ineffective at eliminating the resort to unilateral power when powerful countries want to impose new obligations on others.<sup>38</sup> Therefore it has proven difficult to address the power imbalance between developed and developing countries even within the WTO's current law-based system.

Although the legalization of the dispute resolution process is often thought to be a benefit to developing countries,<sup>39</sup> the reality

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"Green Room" negotiations between industrial powers that excluded developing countries).

<sup>37</sup> The current Doha Round is driven by several coalitions of countries that speak for members of the coalitions. Bernard Hoekman, *Cancun: Crisis or Catharsis?*, available at <http://www.sed.manchester.ac.uk/idpm/research/events/wbseminar/CancunCatharsisorCrisis.pdf> (last visited Feb. 21, 2005) (describing the coalitions and their effect on the negotiations). The coalitions are overlapping and shifting, and WTO members frequently try to negotiate separately with members of a coalition in order to influence the strength of the demands of the coalition. *Id.* See AMRITA NARLIKAR, INTERNATIONAL TRADE AND DEVELOPING COUNTRIES: BARGAINING COALITIONS IN THE GATT/WTO SYSTEM (2003); JANE FORD, A SOCIAL THEORY OF THE WTO: TRADING CULTURES (2003).

<sup>38</sup> See generally Peter Drahos, *Securing the Future of Intellectual Property: Intellectual Property Owners and their Nodally Coordinated Enforcement Pyramid*, 36 CASE W. RES. J. INT'L L. \_\_ (forthcoming 2005) (describing the use of unilateral actions and bilateral agreements to break coalitions and choose enforcement targets. The United States has used bilateral and regional agreements in order to bring the countries more line with its own domestic provisions, therefore bypassing some of the more flexible provisions contained in the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS)). See generally Carlos Correa, *Bilateralism in Intellectual Property: Defeating the WTO System for Access to Medicines*, 36 CASE W. RES. J. INT'L L. \_\_ (forthcoming 2005) (reviewing how United States negotiations with Central America have resulted in an attempt to heighten intellectual property standards in developing countries).

<sup>39</sup> See generally THE URUGUAY ROUND AND BEYOND: THE FINAL REPORT FROM THE FORD FOUNDATION SUPPORTED PROJECT ON DEVELOPING COUNTRIES AND THE GLOBAL TRADING SYSTEM (1989) [hereinafter FORD FOUNDATION REPORT] (noting that benefits to developing countries from a multilateral trading system depend largely on gains from the disciplines of an effective rules-based multilateral system); T.N. SRINIVASAN, DEVELOPING COUNTRIES AND THE MULTILATERAL TRADING SYSTEM: FROM THE GATT TO THE URUGUAY ROUND AND THE FUTURE 57 (1998); Kofi Oteng Kufuor, *From GATT to the WTO: The Developing Countries and the Reform of the Procedures for the Settlement of International Trade Disputes*, 31 J. WORLD TRADE 117, 132-140 (1997).

is not so simple. There is ample evidence that the dispute settlement system created under the Dispute Settlement Understanding (DSU)<sup>40</sup> is not a meaningful source of power for developing countries;<sup>41</sup> to the contrary, the system may asymmetrically favor the developed countries.<sup>42</sup> Small countries often lack the incentive to seek redress.<sup>43</sup> The level of a country's development still heavily influences the settlement of disputes before litigation,<sup>44</sup> and enforcement of obligations depends on

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<sup>40</sup> See *supra* note 2.

<sup>41</sup> Busch & Reinhardt, *supra* note 2, at 719-20 (asserting that the new legalistic architecture of the WTO offers little additional benefit to developing countries because poorer countries have not secured significantly greater responses under the DSU than under the prior dispute settlement system).

<sup>42</sup> Developing countries have difficulty effectively negotiating in the "shadow of the law" because they face adversaries with an incentive to litigate fully, they often face multiple parties, and they have fewer legal resources at their disposal. Marc L. Busch & Eric Reinhardt, "Testing International Trade Law: Empirical Studies of GATT/WTO Dispute Settlement," in *THE POLITICAL ECONOMY OF INTERNATIONAL TRADE LAW: ESSAYS IN HONOR OF ROBERT HUDEC* 466 (Daniel M. Kennedy & James D. Southwick eds., 2002) (finding that developing countries increased from 8 percent to 37 percent of the defendant pool in the GATT versus the WTO eras). With less legal capacity and higher transaction costs relative to the gains from winnings the case, their incentive to settle cheaply is likely to be great. *Id.*; GREGORY SHAFFER, *DEFENDING INTERESTS: PUBLIC-PRIVATE PARTNERSHIPS IN WTO LITIGATION* 157-158 (2003); Gregory Shaffer, *How to Make the WTO Dispute Settlement System Work for Developing Countries: Some Proactive Developing Country Strategies in TOWARDS A DEVELOPMENT-SUPPORTIVE DISPUTE SETTLEMENT SYSTEM IN THE WTO* (ICTSD 2003), available at [http://www.ictsd.org/pubs/ictsd\\_series/resource\\_papers/DSU\\_2003.pdf](http://www.ictsd.org/pubs/ictsd_series/resource_papers/DSU_2003.pdf) (last visited Feb. 21, 2005) (documenting problems that developing countries have in using the dispute settlement system and their lack of use, and recommending reforms); Gregory Shaffer, *Recognizing Public Goods in WTO Dispute Settlement: Who Participates? Who Decides? The Case of TRIPS and Pharmaceutical Patent Protection*, 7 *J. OF INT. ECON. L.* 459 (2004).

<sup>43</sup> See generally Chad P. Bown, *Participation in WTO Dispute Settlement: Complainants, Interested Parties, and Free Riders* (unpublished working paper, on file with authors) (finding that the incentive to participate in a case is related to the amount of affected exports, retaliatory ability, and legal capacity).

<sup>44</sup> See Busch & Reinhardt, *supra* note 2, at 730. Although Australia and India had nearly identical GDP's in 2000, their per capita income levels, and their resulting ability to control the process of legal actions are quite different. *Id.* India, with a per capita income level of US\$ 459, would have a 41 percent chance of getting the average defendant to concede, and Australia, with a per capita income level of US\$ 23,837, would have a 73 percent chance. *Id.* This disparity can be seen even among developing nations. *Id.* For example, Chili and the Philippines have equal GDPs. *Id.* However, holding other variables constant, Chile, with a per capita income of \$5,000 (four times

designing retaliation that imposes realistic costs on a non-complying country.<sup>45</sup> Although the DSU has significantly improved the WTO dispute settlement process for developing country complainants by instituting a more timely “trial,” removing the threat that a defendant could block a case, and providing the option of appellate review (to improve consistency and greater systemization), the reforms have also increased the transaction costs of settling disputes.<sup>46</sup>

Whatever the reality now, over the last six decades developing countries have had a healthy distrust of the GATT/WTO regime and have maintained skepticism about the value of the WTO to their own interests.<sup>47</sup> Integrating developing countries into the WTO regime has essentially been a task of finding a way to incorporate the powerless into a multilateral system whose benefits are distributed on the basis of power.<sup>48</sup> This is required

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that of the Philippines), would have a 60.5 percent chance of obtaining full concessions from a typical defendant, whereas the Philippines would have only a 47.5 percent chance in an otherwise identical case. *Id.*

<sup>45</sup> See generally Naboth van den Broek, *Power Paradoxes in Enforcement and Implementation of World Trade Organization Dispute Settlement Reports*, 37 J. WORLD TRADE 127 (2003) (assessing the role of power in determining compliance with decisions in dispute settlement).

<sup>46</sup> Busch & Reinhardt, *supra* note 2, at 721-22 (observing that in moving from a power-oriented system under the GATT to a more rule-oriented system under the WTO and the DSU, in which legal preparation carries more weight in pre-Panel bargaining, this new premium on legal capacity under the DSU is less burdensome to advanced industrial states who already maintain large, dedicated, and permanent legal and economic staffs to oversee WTO and trade law matters, whereas for poorer countries this move compounds a traditional source of weakness, the lack of market size and therefore retaliatory power, with a new one: legal capacity).

<sup>47</sup> The problems of the small economies are explored in Frank J. Garcia, *Trade and Inequality: Economic Justice and the Developing World*, 21 MICH. J. INT'L L. 975, 985-88 (2000). See generally PETER GALLAGHER, *GUIDE TO THE WTO AND DEVELOPING COUNTRIES* (2000) (providing an understanding of how developing countries work within the WTO and offering case studies on how some developing country members are making progress in working with the obligations and the benefits provided to them under the WTO agreements); RICHARD L. BERNAL, *THE INTEGRATION OF SMALL ECONOMIES IN THE FREE TRADE AREAS OF THE AMERICAS*, IX Policy Papers on the Americas, Study 1 (Center for Strategic and International Studies, Feb. 2, 1998) (examining, in a narrower but relevant context, the issues surrounding the integration of smaller economies into the Free Trade Area of the Americas); *EMERGING MARKET ECONOMIES, GLOBALIZATION AND DEVELOPMENT* (Grzegorz W. Kolodko ed., 2003) (examining the development of emerging market economies).

<sup>48</sup> Garcia, *supra* note 47, at 985.

not only to bring developing countries into the regime, and to improve the universality of the regime, but also to maintain a power balance in the regime as it matures.<sup>49</sup> The GATT/WTO regime is simultaneously strong and fragile. Its long run stability depends on insuring that all members continue to believe that the benefits of belonging to the WTO outweigh the costs, and this means that the powerless must continue to feel that they are better off within the organization than outside of it.<sup>50</sup>

Historically, the primary issue between developed and developing countries has been whether the principle that governed GATT was to be one of formal equality (despite the differences between developed and developing countries) or real equality – recognizing that formal equality between countries that are unequal is not equality.<sup>51</sup> Although the initial U.S. position on this question was that formal equality should be the rule, eventually the United States had to succumb to the view that if it wanted the GATT/WTO system to be attractive to all countries it would have to bend toward real equality.<sup>52</sup> The developing countries had no interest in participating in a system that did not acknowledge the special position of poor countries, and the insistence of the United States that poor countries make the same sort of “concessions” as wealthy countries and accept the same sort of obligations made membership unattractive.<sup>53</sup> Over time, the benefits of universality began to outweigh the desire for a uniform approach to rights and obligations, and the United States, as well as the rest of the developed world, began to understand the importance of creating special rules that would acknowledge the different status of the poorer countries.<sup>54</sup> As Robert Hudec has written:

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<sup>49</sup> *Id.* at 987.

<sup>50</sup> *Id.* at 987, 993.

<sup>51</sup> *Id.*

<sup>52</sup> This is the central theme in ROBERT E. HUDEC, *DEVELOPING COUNTRIES IN THE GATT LEGAL SYSTEM* 17 (1987). See also FORD FOUNDATION REPORT, *supra* note 39, at I, J (summarizing how tensions between developed and developing countries over trade matters accumulated in the post-war years) and at 15-23 (exploring the development strategies, political and other factors underlying protectionism, and multilateral negotiation that contributed to these tensions).

<sup>53</sup> Gerald M. Meier, *The Tokyo Round of Multilateral Trade Negotiations and the Developing Countries*, 13 *CORN. INT'L L. J.* 239, 253 (1980).

<sup>54</sup> FORD FOUNDATION REPORT, *supra* note 39, at 37-38.



The history [of developing country involvement in the GATT/WTO system], begins with a legal relationship based essentially on parity of obligation, with only very limited, almost token, exceptions. Over the years, the relationship has gravitated, in seemingly inexorable fashion, towards the one-sided welfare relationship demanded by the developing countries.<sup>55</sup>

Ultimately, the WTO implemented the concept of Special and Differential treatment – the notion that within the GATT/WTO system, poor countries would be given treatment that reflected their poverty, and thus their relative lack of bargaining power.<sup>56</sup> Two types of special treatment developed.<sup>57</sup> From the standpoint of avoiding obligations, commitments made by developed countries would be implemented more slowly, or less severely, for developing countries, and developing countries would not have to make the same concessions as industrial country members.<sup>58</sup> From the standpoint of receiving special privileges, the industrial and developing countries negotiated the GSP program.<sup>59</sup> Under this program, developed countries were allowed and encouraged to

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<sup>55</sup> HUDEC, *supra* note 52, at 4.

<sup>56</sup> FORD FOUNDATION REPORT, *supra* note 39, at 23-29 and app. C (describing how the rules for special and differential treatments for developing countries evolved in the GATT). Briefly in 1965, following the 1958 Haberler Report and as a result of developing countries' initiatives in the early and mid-1960's, Articles 36, 37, and 38 were added to GATT as Part IV (Trade and Development); they are devoted solely to the problems of developing countries. *Id.* Article 36 of GATT, for example, recognizes the new principle of non-reciprocity between developed and developing countries. *Id.* at 993; *see generally* Garcia, *supra* note 47, at 988 (describing the evolution of special and differential treatment).

<sup>57</sup> FORD FOUNDATION REPORT, *supra* note 39, at 39. Special and differential treatment was comprised of two broad elements: trade preferences in developed country markets and special rights to maintain barriers at home. *Id.*

<sup>58</sup> *Id.*

<sup>59</sup> Meier, *supra* note 53, at 240. The GSP was instituted during the Tokyo Round of Multilateral Trade Negotiations, which ended in 1979. *Id.* Developing countries had long demanded that industrially advanced countries grant tariff preferences on manufactured and semi-manufactured goods imported from poorer countries, while industrial countries had often balked at giving trade preferences for a variety of reasons. *Id.* Initial work was undertaken under the auspices of UNCTAD, the United Nations Conference on Trade and Development, through two UNCTAD conferences. *Id.* A Specialized UNCTAD Trade and Development Board, established in 1970, developed the framework that led to the successful incorporation of the GSP program at the WTO. *Id.*

give preferential market access to the developing countries by lowering tariffs for developing countries below the level of tariffs for developed countries.<sup>60</sup>

In the absence of any official authorization, preferences given under the GSP program to developing, but not developed, countries would have violated the prohibition on discriminatory treatment contained in the "cornerstone" most favored nation (MFN) obligation of Article 1 of GATT.<sup>61</sup> Accordingly, the members created the necessary exception to the MFN requirement to allow such preferences in two ways: First, by way of a waiver of Article 1, known as the 1971 GSP Decision,<sup>62</sup> and later by way of a 1979 decision<sup>63</sup> that became known as the 1979 Enabling

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<sup>60</sup> Yusuf, *supra* note 16, at 488-90. After the GSP system was launched in the WTO in 1971, The Trade Negotiations Committee established a "Framework" group in November 1976 during the Tokyo Round because the developing countries were demanding a permanent legal basis for preferences in the GATT system. *Id.* The purpose of this Framework Committee was to "negotiate improvements in the international frameworks for the conduct of world trade, particularly with respect to trade between developed and developing countries and for differential and more favorable treatment to be adopted in such trade." GATT, Doc. MTN/17, ¶1 (Nov. 8, 1976) *cited in* Yusuf, *supra* note 16, at 488-490. One of the major achievements of this group was the Text of the Enabling Clause, thus establishing a permanent legal framework. *Id.* at 488-490.

<sup>61</sup> General Agreement on Tariffs and Trade, Oct. 30, 1947, 61 Stat. A-11, T.I.A.S. 1700, 55 U.N.T.S. 194 [hereinafter GATT]. Article 1:1 prohibits discrimination between members, stating that "any advantage, favor, privilege, or immunity granted by any member 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." *Id.* Therefore, under this provision, the lower tariffs given to one country must be given to all member countries. *Id.*

<sup>62</sup> See Contracting Parties, *Generalized System of Preferences*, B.I.S.D. 18S/24, ¶a (June 25, 1971) [hereinafter 1971 Waiver]. The 1971 GSP Decision granted a special GATT waiver providing the initial authorization to enable developed countries to grant preferences to developing countries without granting the same preferences to other members:

Without prejudice to any other Article of the General Agreement, the provisions of Article I shall be waived for a period of ten years to the extent necessary to permit developed contracting parties, subject to the procedures set out hereunder, to accord preferential tariff treatment to products originating in developing countries and territories with a view to extending to such countries and territories generally the preferential tariff treatment referred to in the Preamble to this Decision, without according such treatment to like products of other contracting parties. *Id.*

<sup>63</sup> GATT Contracting Parties, *Decision on Differential and More Favorable*

Clause.<sup>64</sup> The Enabling Clause continues to provide the legal basis for the MFN exception allowing countries to give the preferences, thus serving as the instrument that determines whether preference programs are lawful.<sup>65</sup>

In sum, the GSP system was instituted in the hope that developing countries could use the trade preferences to increase their national wealth and thereby increase their interest in, and allegiance to, the GATT/WTO regime.<sup>66</sup> The underlying theory was that the preferences would hasten the economic development of less developed countries and would increase the power that these countries would derive from their own economic strength.<sup>67</sup> This, in turn, would help to restore and maintain balance within the system.<sup>68</sup> In this way, the preferences can be seen as a reflection of, and reaction to, the economic and political situation in the recipient countries.<sup>69</sup> Nonetheless, the GSP system has unique characteristics that make it an imperfect tool for achieving that goal.<sup>70</sup>

### *B. Power and the GSP System*

Four characteristics of the GSP system inform our analysis. First, each donor country determines, within the context of the Enabling Clause, what preferences it will give and under what circumstances; accordingly, the U.S. GSP program is unlike the program of the European Community (EC), and Japan's program is different still.<sup>71</sup> The lack of coordination of the programs gives

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*Treatment, Reciprocity, and Fuller Participation of Developing Countries*, Nov. 28, 1979, GATT B.I.S.D. 203 (1980) [hereinafter Enabling Clause].

<sup>64</sup> See generally Yusuf, *supra* note 16, at 488-489; Meier, *supra* note 53, at 249; Bela Belassa, *The Tokyo Round and the Developing Countries*, 14 J. WORLD TRADE L. 93, 97 (1980).

<sup>65</sup> See Enabling Clause, *supra* note 63.

<sup>66</sup> See Belassa, *supra* note 64, at 97-107.

<sup>67</sup> U.S. General Accounting Office (GAO), Report to the Chairman, Subcommittee on Trade, Committee on Ways and Means, House of Representatives, Letter to the Chairman, p. 1., June 2001 [hereinafter GAO REPORT].

<sup>68</sup> *Id.*

<sup>69</sup> See *id.* at 2.

<sup>70</sup> See *id.* at 4.

<sup>71</sup> *Id.* For example, the U.S. program offers duty-free entry for the products under its preference scheme, while the EC's program provides for either duty free entry or

the preferences a scattershot appearance, given that the products granted preferential treatment by the United States may not get preferential treatment from the European Community. It also means that the terms and conditions under which preferences are given are quite diverse.<sup>72</sup>

Second, the donor countries do not have to give the preferences - they are purely donative - and recipient countries have no legal right to insist on the preferences.<sup>73</sup> Accordingly, donor countries are free to withdraw their preferences at any time without fear of retribution, and with no resulting legal remedy for the recipient countries.<sup>74</sup> The preferences are considered gifts, and whether donor countries continue those preferences depends largely on whether the long term goal of the program—to integrate the developing countries into the WTO system—continues to be

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reduced tariffs. *Id.* Further the EC's program applies to more countries than does that of the United State's. *Id.* at 5. Both the United States and EC established GSP programs in the early 1970s, offering trade preferences to only 100 developing countries. *Id.* Presently, the United States offers nonreciprocal trade preferences to 151 countries and territories, while the EC offers preferences to 171 countries. *Id.* Moreover, unlike the United States, the EC has also expanded the number of products that are eligible for the preferences. *Id.*

<sup>72</sup> *Id.* at 5-7.

<sup>73</sup> The 1971 Waiver made this non-commitment explicit: "Noting the statement of developed contracting parties that the grant of tariff preferences does not constitute a binding commitment and that they are temporary in nature." See 1971 Waiver, *supra* note 62. See also, 1982 REPORT BY THE SECRETARY-GENERAL OF UNCTAD, ASSESSMENT OF THE RESULTS OF THE MULTILATERAL TRADE NEGOTIATIONS, UNCTAD DOC. T/B/778/Rev., 29, ¶176 (1982) (finding that the key provision of the Enabling Clause that allows more favorable treatment to developing countries also imposes no obligation on developed countries to accord this differential treatment). One portion of the Appellate Body's opinion in EC-Preferences appears to be to the contrary, because the Appellate Body said that "the characterization of the Enabling Clause as an exception in no way diminishes the right of Members to provide or to receive 'differential and more favorable treatment.'" AB REPORT, *supra* note 4, ¶98. In context, because the Appellate Body is discussing the nature of the Enabling Clause as an exception of the MFN provision, this statement does not affirm the right of any country to insist that another country give it preferences. *Id.* This passage only confirms that right of countries to insist that countries giving preferences do so under the authority, and within the limits of, the Enabling Clause, which establishes the right to violate the MFN provision. *Id.*

<sup>74</sup> GAO REPORT, *supra* note 67, at 11-12. Many donor countries, of course, enact their preferences for a period of years, giving the programs some stability, subject only to provisions that allow the preferences to be withdrawn in sectors where imports account for a large share of the market. *Id.*

important and worthwhile in their eyes.<sup>75</sup>

Third, and correlatively, the recipient countries do not have to accept the preferential treatment under the program.<sup>76</sup> If the preferences do not meet their needs, or are otherwise undesired, the recipient countries are free to reject them and plan their affairs as if the preferences did not exist.<sup>77</sup>

Finally, the fourth characteristic of the GSP programs follows from the fact that preferences are gifts.<sup>78</sup> Soon after GSP programs were initiated, donor countries began making the preferences conditional on various factors, requiring the recipient countries to meet one or more tests as a condition of receiving the preferences.<sup>79</sup> Over time, the donor countries imposed increasingly stringent conditions for the receipt of the preferential treatment, requiring the recipient country to change fundamental national policies in order to get the preferences.<sup>80</sup> These conditions were of two types. The so-called “negative conditions” are those conditions that a country must meet in order to qualify for GSP preferences in the first place.<sup>81</sup> The GSP program of the United States is built around negative conditionality, denying GSP preferences to countries that, for example, practice communism (with exceptions), engage in unlawful expropriation, are involved with terrorism, or fail to meet certain standards for labor or intellectual property rights.<sup>82</sup> Other conditional GSP programs involve so called “positive conditionality,” where countries that

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<sup>75</sup> *Id.*

<sup>76</sup> *Id.*

<sup>77</sup> *Id.*

<sup>78</sup> *Id.*

<sup>79</sup> See *infra* notes 125-42 and accompanying text. The conditions presently imposed by the United States include requirements concerning the recipient countries' policies with respect to labor rights and intellectual property rights. See Office of the United States Trade Representative, Executive Office of the President, *U.S. Generalized System of Preferences Guidebook*, 23-24 (Mar. 1999), at <http://www.ustr.gov/reports/gsp/index.html>. For a comprehensive study of the effect of the U.S. labor policy conditions on labor rights in developing countries, see Lance Compa & Jeffrey S. Vogt, *Labor Rights in the Generalized System of Preferences*, 22 COMP. LAB. L. & POL'Y J. 199 (2001).

<sup>80</sup> See, e.g., GAO REPORT, *supra* note 67, at 11-12.

<sup>81</sup> Howse et al., *Internet Roundtable*, *supra* note 12, at 245.

<sup>82</sup> *Id.*

meet certain conditions are given extra preferences over and above those that are given generally to developing countries.<sup>83</sup> The preferences challenged by India in the *European Conditions* case are examples of positive conditionality.<sup>84</sup>

On one level, the conditions that donor countries placed on GSP recipients were not surprising. Some conditions were designed simply to insure that the program was not abused; recipient countries must, for example, follow stringent "country of origin" requirements to make sure that the goods were made in, and not just transshipped through, the recipient country.<sup>85</sup> Moreover, the conditions were not unnatural; they reflected the fact that those who give gifts often feel as if they should be able to control the recipient in various ways.<sup>86</sup> As the conditions placed on recipient countries grew in number and severity, however, and as the conditions appeared to move further and further away from the rationale for giving preferences in the first place, conditional preferences began to be a source of friction between donor and recipient countries.<sup>87</sup>

The friction between developed and developing countries over GSP programs comes from several sources.<sup>88</sup> The value of the preferences has eroded as countries lowered their tariffs to all WTO members in successive rounds of negotiations. Lower levels of general tariffs meant that preferential treatment did not give

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<sup>83</sup> *Id.*

<sup>84</sup> *Id.*

<sup>85</sup> See, e.g., *Comprehensive Review of the Generalized System of Preferences*, Report by the UNCTAD Secretariat 39, UN Doc. No TD/B/C.5/63 (Apr. 9, 1979), in UN TDBOR, *Operation and Effects of the Generalized System of Preferences* 19, Doc. TD/B/C.5/71 (1981) (regarding conditions that donor countries place on GSP recipients); UN Conference on Trade and Development, 9 Sess., Midrand Declaration and a Partnership for Growth and Development 12, UN Doc. TD/377 (May 24, 1996).

<sup>86</sup> Howse et al., *Internet Roundtable*, *supra* note 12.

<sup>87</sup> *Id.*

<sup>88</sup> *Id.*

<sup>88</sup> See GAO REPORT, *supra* note 67. Recently, a group of eminent persons appointed by the Director-General of the WTO to mark the tenth anniversary of the WTO has criticized the GSP programs because the conditions erode the benefits of the programs, because the programs reflect the interests of donor, not donee nations, and because the programs have become quite complex and lack stability. See *The Future of the WTO, Addressing Institutional Challenges in the New Millennium*, (Peter Sutherland, Chair, 2004).

developing countries much of a competitive advantage.<sup>89</sup> The preferences were often given on products of little interest to exporters in the developing countries, and were withheld on products that the countries could have successfully exported.<sup>90</sup> If recipient countries become too successful, and for example, lose developing country status, donor countries may withdraw preferences. Additionally, preferences can be withdrawn from individual goods when they reach certain threshold amounts.<sup>91</sup>

In the context of the frictions generated by these issues, India's challenge to the EC program presented both legal and political issues, and resulted in great interest in the *EC—Conditional Preference* case.<sup>92</sup> A threshold issue is whether the conditions under which preferences are given should be subject to judicial control, or whether conflicts over the conditions are susceptible

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<sup>89</sup> GALLAGHER, *supra* note 47, at 112-114. There has been an erosion of preference margins beginning with the Tokyo Round, where an average cut of one third in industrial country tariffs reduced preference margins, and again in the Uruguay Round where preference margins were cut by another 40 percent. *Id.* Further, while developed nations have begrudgingly granted preferences, due to a rise of New Protectionism since the Tokyo Declaration in 1973, the effectiveness of these preferences has always been limited by the use of exemptions, tariff quotas, and escape clauses. Meier, *supra* note 53, at 240; *see also* FORD FOUNDATION REPORT, *supra* note 39, at 39 (finding that while developing countries have benefited from the GSP, those benefits have been counteracted by small preference margins, limited product coverage, and the graduation of many developing countries); *see* Horst Kohler, Working for a Better Globalization, Address at the United States Conference of Catholic Bishops (Jan. 28, 2002) (transcript available at <http://www.imf.org/external/np/speeches/2002/012802.htm> (last visited Feb. 21, 2005)).

<sup>90</sup> *See generally* GALLAGHER, *supra* note 47 (discussing the practical application of preferences).

<sup>91</sup> *Id.* *See also* GAO REPORT, *supra* note 67 (regarding preferences and their privileges).

<sup>92</sup> *See* Daniel Pruzin, *WTO Panel Rejects EU Linking GSP Benefits With Policies on Environment, Labor, Drugs*, WORLD NEWS (Vol. 20, No. 36) 1490, 1491 (2003). The initial substantive and political importance of this case is highlighted by the fact that seventeen developing countries and the U.S. requested to be third parties. *See European Communities – Conditions for the Granting of Tariff Preferences to Developing Countries – Constitution of the Panel Established at the Request of India*, WT/DS246/5 (Mar. 6, 2003). In its third party submission, the United States stated that it desired to participate in this proceeding because of the importance of the issues presented. *Id.* The United States understood the systemic implications of the dispute between the EC and India. *European Communities – Conditions for the Granting of Trade Preferences to Developing Countries – Third Party Submission of the United States*, WT/DS246 (Apr. 30, 2003).

only to political resolution.<sup>93</sup> To some, the nature of the preference programs makes controversies about their operation largely political, not legal, questions.<sup>94</sup> Even if issues surrounding the GSP program were subject to judicial review—that is, even if the Enabling Clause were interpreted to consist of standards that GSP programs must meet in order to amount to a permitted violation of the MFN principle—further problems would arise.<sup>95</sup> As a matter of legal interpretation, the Appellate Body had to construe the Enabling Clause to determine the contours of the legal rules that constrain GSP programs, and then determine whether any conditional preferences that ran afoul of the Enabling Clause might be held to be lawful under the general defensive provisions of Article XX of GATT.<sup>96</sup>

The legal issues raised in these inquiries are difficult enough, but they must also be understood in light of the political relationship between developed and developing countries. Because industrial countries are not required to give preferences,<sup>97</sup> any attempt by the Appellate Body to interpret the Enabling Clause to restrict the conditions under which the preferences are given could result in the loss of the preferences altogether. A country that is not allowed to shape its own preference program may feel inclined to simply abandon the program, willing to face the displeasure of the developing countries in order to enforce its own sense of control.<sup>98</sup> As a result, the interpretive challenges presented by conditional preferences must be undertaken with the recognition that any interpretation will affect the political relationship between developed and developing countries, the willingness of developed countries to grant the preferences, and the loyalty of the developing countries to the systemic values of the WTO system.<sup>99</sup>

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<sup>93</sup> See Daniel Pruzin, *supra* note 92, at 1491.

<sup>94</sup> See, e.g., Howse et al., *Internet Roundtable*, *supra* note 12, at 246-48; Howse, *India's WTO Challenge*, *supra* note 12, at 387-399.

<sup>95</sup> See Howse, *Back to Court After Shrimp/Turtle*, *supra* note 12, at 1367-78.

<sup>96</sup> GATT, June 1986, Art. XX (allowing countries to avoid their WTO obligations in order to meet specified non-trade goals, such as protection of public health or the environment, provided that the country is able to meet stringent jurisprudential hurdles).

<sup>97</sup> See *supra* note 38 and accompanying text.

<sup>98</sup> AB REPORT, *supra* note 4.

<sup>99</sup> See *id.*



The GSP program in general, and its continuation through the Enabling Clause, are both products of political compromise. Like many WTO provisions, the legal framework of the GSP system is steeped in ambiguity, with a vast range of issues on which there has been no true meeting of the minds. It may be true, as Professor Howse has pointed out, that developed countries never accepted the notion that they could not pick and choose the conditions on which they would implement their GSP programs,<sup>100</sup> but it is equally true that developing countries have never accepted the notion that any condition put on the programs is permissible.<sup>101</sup> In fact, the developing and developed countries have never been able to decide on more than the general principles of the Enabling Clause, and have had no basis for agreeing on the details of multilateral oversight of the program.<sup>102</sup> The question thus becomes whether these disparate perceptions of the GSP program should invite or repel the neutral involvement of the Appellate Body.<sup>103</sup> If involvement is necessary, then how should the Appellate Body use its interpretive powers? The *EC-Conditional Preferences* case posed both of these questions

### III. The Problem of Conditional Preferences

The conditions placed on preferences by donor countries mean

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<sup>100</sup> See Howse, *India's WTO Challenge*, *supra* note 12, at 393. Even the evidence on this point is ambiguous. Professor Howse cites a statement from a trade diplomat that "it was tacitly agreed that any donor country would have the powers to extend the preferential treatment to any country or to withdraw this treatment if there should be any valid reason for this in the opinion of the preference-giving country." *Id.* Aside from the fact that this personal opinion is far removed from the normal evidence of negotiating intent, the statement leaves ambiguous the role of the donor state in determining the "valid reason" for withholding benefits. It could very well be that the drafters contemplated that the reasons for withholding benefits were collectively assumed while the determination of whether a legitimate reason was in fact present was to be determined by each country. Naturally, when a condition is legitimate—as when the preference depends on goods coming from that country—the donor country should be given great discretion in making that determination. That does not necessarily give the donor country total discretion to determine which conditions are legitimate and which are not.

<sup>101</sup> See Howse, *Back to Court after Shrimp/Turtle*, *supra* note 12 (discussing developing and developed countries inability to decide on more than the general principles of the Enabling Clause).

<sup>102</sup> *Id.*

<sup>103</sup> *Id.*

that the preferences are essentially conditional gifts. Therefore, to gain a better understanding of the role GSP preferences play in the WTO system, it is helpful to explore the general legal approach to conditional gifts. Conditional gifts are those given on the condition that the recipient change its behavior in some way. For example, donors to universities give money for particular purposes, making those purposes a condition of the gift. A donor might, for example, give a gift to support the teaching of history, conditioned on the inclusion of a certain theory of history. People planning their estates often make their bequests conditioned on the behavior of the beneficiary of the gifts; a person might leave a bequest to a favored nephew, conditioned on the nephew going into a drug rehabilitation program. The government often conditions the benefits that it makes available on certain behavior in the recipient, making, for example, the grant of welfare conditioned on the recipient seeking a job. In all the examples, like preferences under the General System of Preferences, the gift is dependent on some change in behavior.

In most such cases, of course, as long as the condition that is placed on the gift is germane to the gift's purpose, the conditions are not troublesome. We expect donors to be able to determine the purposes of their gifts and make sure that the purposes are in fact fulfilled. Because the donor need not make the gift, and because the recipient need not accept the gift, the conditions put on most gifts ensure that the joint expectations of the donor and recipient are observed. Indeed, any legal restraint on such gifts appears at first glance to be paradoxical. Arguably, conditional gifts are better than no gifts at all; accordingly, the right to withhold the gift and confer no benefit on the recipient would seem to imply that the donor should also have the right to reduce the benefit by imposing some condition on the gift. The greater right (to deny the gift in the first place) would seem to imply the lesser right (the right to condition the gift as the donor wants).

Yet, legal systems often intervene to review and control the conditions that donors put on their gifts. It is common, for example, to strike down government benefits that are conditioned on the recipient giving up a constitutional right that the recipient would otherwise have.<sup>104</sup> For example, it is impermissible for the

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<sup>104</sup> LAWRENCE H. TRIBE, *AMERICAN CONSTITUTIONAL LAW* 681 (2d ed. 1988).

government to condition unemployment compensation on the recipient's agreement to work on the Saturday Sabbath,<sup>105</sup> or to condition public broadcasting subsidies on the broadcaster's agreement to avoid editorial comment.<sup>106</sup> Similarly, courts strike down conditions imposed on bequests when those conditions are against public policy.<sup>107</sup> A donor may not condition a gift on the recipient's agreement to marry within the faith or to get a divorce.<sup>108</sup>

In short, mature legal systems recognize limits on the power of donors to do indirectly—through conditional gifts—what they may not do directly, and they recognize the autonomy of recipients by striking down conditional gifts that would threaten that autonomy in important ways.

The reason for these limitations is directly related to the central concern of the analysis here: the division of power between donors and recipients. In her magisterial exploration of the doctrine of unconstitutional conditions,<sup>109</sup> Kathleen Sullivan has identified the balance of power as the central theme in cases striking down

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<sup>105</sup> See generally *Hobbie v. Unemployment Appeals Comm'n*, 480 U.S. 136 (1987) (concluding that that the Unemployment Appeals Commission's disqualification of the employee from receipt of benefits violated the Free Exercise Clause of the First Amendment, applicable to the states through the Fourteenth Amendment).

<sup>106</sup> See generally *F.C.C. v. League of Women Voters*, 468 U.S. 364 (1984) (determining that restrictions on free speech in public broadcasting were upheld only if the restrictions were narrowly tailored to further a substantial governmental interest).

<sup>107</sup> For examples where courts struck down conditions because they were against public policy, see *Estate of Robertson v. U. S.*, 903 F.2d 1034 (5 Cir. 1990); *In re Estate of Kirkendall*, 642 N.E. 2d 548 (Ind. Ct. App. 1994); *In re Estate of Mank*, 699 N.E. 2d 1103 (Ill. App.1998), *appeal denied*, 181 Ill. 2d 497 (1998); *In re Liberman*, 18 N.E. 2d 658 (N.Y. 1939). See generally Ian Johnson, *Conditions Not to Dispute Wills and the Inheritance Act of 1975*, 25 LIVERPOOL L. REV. 71 (2004) (discussing conditions on bequests that are against public policy).

<sup>108</sup> See generally *Helms v. Helten*, 290 N.W. 2d 876 (1980) (striking down condition on gift to son "as long as he refrains from marrying or associating with in any way his common law wife").

<sup>109</sup> Kathleen M. Sullivan, *Unconstitutional Conditions*, 102 HARV. L. REV. 1415 (1989); see generally Jason Mazzone, *The Waiver Paradox*, 97 NW. U. L. REV. 801 (2003) (attempting to reconcile the doctrine of unconstitutional conditions on government benefits with the waiver of constitutional rights in criminal cases).

conditions placed on government grants or subsidies.<sup>110</sup> The notion that government may not condition its gifts in ways that interfere with important constitutional liberties does “not simply protect individual rightsholders piecemeal. . . [it] also help[s] determine the overall distribution of power between governments and rightsholders generally, and among classes of rightsholders.”<sup>111</sup> The distribution and use of power from a systemic perspective is at the heart of understanding limitations on conditional gifts.<sup>112</sup>

Admittedly, the power of courts to strike down conditions on government grants or subsidies as unconstitutional is rooted in the positive rights guaranteed by the Constitution, while the WTO system gives recipient countries no such explicit claim to be left alone.<sup>113</sup> Similarly, the power of courts to strike down conditions on bequests is rooted in well-defined notions of individual autonomy that can be reversed by democratic legislation if wrongly decided. Arguably, in the international realm, where there are no well-defined principles with which to determine whether any country has the right to be free from interference from any other government, there is no basis for determining when conditions placed on gifts violate “global public policy” or otherwise interfere with the distribution of rights and responsibilities among nations in any defined ways.

Yet we should not overestimate the importance of those differences. The international system is created around norms

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<sup>110</sup> Cases striking down conditions placed on private gifts are more likely to refer to public policy limitation on conditions rather than to power-based analysis of such conditions. See generally Johnson, *supra* note 107 (discussing conditions on bequests that are against public policy). Nonetheless, preserving the autonomy of the recipient to make important decisions without having to worry about the power exercised by the donor’s promise of riches is not far from the surface of these cases. *Id.*

<sup>111</sup> Sullivan, *supra* note 109, at 1490.

<sup>112</sup> For example, power is at the heart of the theory of coercion that is so often invoked when unconstitutional conditions are struck down. Thus, the U.S. Supreme Court has found that the attachment to a privilege is coercive when “[i]n reality, the carrier is given no choice, except a choice between the rock and the whirlpool,—an option to forego a privilege which may be vital to his livelihood or submit to a requirement which may constitute an intolerable burden.” Sullivan, *supra* note 109, at 1430 (quoting Justice Sutherland in *Frost Trucking Co. v. R.R. Comm’n*, 271 U.S. 583 (1926)).

<sup>113</sup> See generally Sullivan, *supra* note 109 (discussing unconstitutional conditions).

governing the behavior of one state to another and it is grounded in the right to be left alone—the basis of sovereignty.<sup>114</sup> The countries of the world have developed recognizable modes of behavior toward one another that provide a basis for recognizing the limits to which power can be used in the international system.<sup>115</sup> It is not far fetched to suggest that the WTO system must pay attention to those modes of behavior and implicit rights when it addresses the question of which conditions placed on GSP preferences are permissible and which ought to be beyond the pale.

Moreover, two of the basic norms of the international community—the prohibition against discrimination between countries and the prohibition of discrimination between nationals and non-nationals—are explicit in WTO treaties.<sup>116</sup> Certainly, WTO members have the right to rely on a promise of equal treatment as a basic norm that will govern relationships between members.<sup>117</sup>

If nothing else, the survival of the WTO regime itself will depend on the ability of the system to maintain balance between the interests of the WTO members,<sup>118</sup> as well as continued faith by all the members that their interests are not subject to arbitrary or norm-violating behavior of other states. The GSP system was designed to provide engagement and balance that are essential to the long run success of the community.<sup>119</sup> It is hard to imagine

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<sup>114</sup> See, e.g., JEREMY RABKIN, WHY SOVEREIGNTY MATTERS 2 (1998) (“Sovereignty denotes independence. A sovereign state is one that acknowledges no superior power over its own government . . .”) and John Jackson, *Sovereignty Modern, A New Approach to an Outdated Concept*, 97 Am. J. Int’l L. 782 (2003) (reviewing various meanings of the concept of sovereignty). For one author’s perspective on the relationship between sovereignty and the WTO see Gerhart, *supra* note 1, at 48-55.

<sup>115</sup> International law thus serves as both a source of limitations on state interference with other states, and as a source of obligations from each state to the international community. See generally IAN BROWNLIE, PRINCIPLES OF PUBLIC INTERNATIONAL LAW (5th ed. 1998) and AMERICAN LAW INSTITUTE, RESTATEMENT OF THE LAW (THIRD) FOREIGN RELATIONS LAW OF THE UNITED STATES, § 102, cmt. B (1987) (discussing the norms that make up customary international law).

<sup>116</sup> GATT, *supra* note 61, Art. I and Art. III.

<sup>117</sup> See Peter M. Gerhart, *Slow Transformations: The WTO As a Distributive Organization*, 17 AM. U. INT’L L. REV. 1045 (2002).

<sup>118</sup> *Id.*

<sup>119</sup> *Id.* at 1053-65.

that WTO members, both developed country members and developing country members, did not intend that the GSP system would become a source of stabilization, rather than destabilization, for the community.

The Enabling Clause should therefore be understood as embodying the systemic values and relational norms that allow the WTO regime to flourish. Undoubtedly, the Enabling Clause needs to be definitely interpreted. It should not, however, be interpreted with the assumption that because GSP preferences are gifts, the donor country may impose any conditions it wants on the behavior of the recipient country. Instead, the Enabling Clause needs to be understood as an important framework for working out the relationship between states with power and those without.

#### **IV. The Decision in European Communities – Conditional Preferences**

##### *A. The European Community's GSP Program*

The *EC—Conditional Preferences* case dealt with one facet of the GSP plan that the European Community adopted in January 2002<sup>120</sup> (EC Council Regulation). Europe's plan provided general tariff preferences to all developing countries (hereinafter the "General Arrangements").<sup>121</sup> Under this Plan, Europe granted "non-sensitive" products duty-free treatment (zero tariffs) and "sensitive" products a tariff rate that was lowered by 3.5 percent points below the generally applicable MFN rate.<sup>122</sup> In addition to the general arrangements, Europe provided additional programs that were available only to certain developing countries. First, under the Special Incentive Arrangements, Europe gave an additional margin of preference to developing countries that the European Commission determined had complied with specified

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<sup>120</sup> Council Regulation 2501/2001 of 10 December 2001, Applying a Scheme of Generalized Tariff Preferences for the Period from 1 January 2002 until 31 December 2004 [hereinafter EC Council Regulation]; see The EU-LDC Network, *EU-LDC Themes – Social, Environmental & Welfare Aspects of Trade Policy* (discussing the relationship between this plan and the European Communities prior plan) available at [http://62.58.77.238/themes/socialwelfare/socialwelfare\\_policy.php](http://62.58.77.238/themes/socialwelfare/socialwelfare_policy.php) (last visited Feb. 21, 2005).

<sup>121</sup> EC Council Regulation, *supra* note 120, at art. 1(2)(a).

<sup>122</sup> *Id.* art. 7.

labor or environmental standards.<sup>123</sup> Qualified countries would benefit from a reduction of 5 percentage points on top of the 3.5 percent point reduction on “sensitive goods” under the General Arrangement—a total of 8.5 percentage points.<sup>124</sup> Under the labor incentives, the additional preferences were available for *all* products from qualified developing countries,<sup>125</sup> while under the environmental incentives, the additional preferences were available only on imports of tropical forest products.<sup>126</sup>

Second, under the Drug Arrangements, Europe gave additional preferences to countries certified as having programs to combat drug production and drug trafficking;<sup>127</sup> for recipient countries the tariffs on “sensitive products” were reduced to zero.<sup>128</sup> Under a third program, Europe gave even more favorable treatment to those countries designated by the United Nations as least developed countries (LDCs).<sup>129</sup>

Significantly, Europe adopted different procedures for granting

<sup>123</sup> *Id.* art. 1(2)(e).

<sup>124</sup> *Id.* art. 8(2).

<sup>125</sup> *Id.* art. 14(2). The special incentive arrangements for the protection of labour rights may be granted to a country the national legislation of which incorporates the substance of the standards laid down in ILO [International Labor Organization] Conventions No. 29 and No. 105 on forced labour, No. 87 and No. 98 on the freedom of association and the right to collective bargaining, No. 100 and No. 111 on non-discrimination in respect of employment and occupation, and No. 138 and No. 182 on child labour and which effectively applies that legislation. *Id.*

<sup>126</sup> *Id.* art. 21(2). The special incentive arrangements for the protection of the environment may be granted to a country which effectively applies national legislation incorporating the substance of internationally acknowledged standards and guidelines concerning sustainable management of tropical forests. *Id.*

<sup>127</sup> *Id.* art. 1(2)(b) & (c).

<sup>128</sup> *Id.* art. 10.

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 . . . *Id.*

<sup>129</sup> *Id.* art. 40. This provision was a continuation of the Regulation (EC) 416/2001 (the EBA Regulation) that the European Council adopted in February 2001, granting duty-free access to imports of all products from LDC's except arms and munitions, without any quantitative restrictions. See User's Guide to the European Union's Scheme of Generalised Tariff Preferences (Feb. 2003), at <http://europa.eu.int/comm/trade/gsp/gspguide.htm>.

the additional preferences to countries with appropriate environmental and labor policies than it did for countries with appropriate drug policies.<sup>130</sup> Under the Special Incentive Arrangements, a developing country could apply for the additional preferences on sensitive products by showing that its regulatory policy complied with certain labor and environmental standards.<sup>131</sup> The applicant country would make a request to the Community, show that it fulfilled the relevant conditions set out under the particular special incentive arrangement, undergo an examination of the situation in its territory, and agree to monitor the application and compliance with the stated labor or environment standard.<sup>132</sup> Compliance was demonstrated by showing adequate measures to formulate legislation regarding the stated standards and the commitment to implement, monitor, and enforce those standards.<sup>133</sup>

By contrast, Europe made no provision in the drug incentive program for countries to apply for the special preferences; nor did it state what standards the applicant country would have to meet to qualify for the drug incentives.<sup>134</sup> Instead, the European Commission itself identified the countries that it would favor with these preferences;<sup>135</sup> it gave the drug preferences to members of

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<sup>130</sup> EC Council Regulation, *supra* note 120.

<sup>131</sup> *Id.* art. 8(1). See also UNCTAD Secretariat, *Quantifying the Benefits Obtained by Developing Countries From The Generalized System of Preferences*, UNCTAD/ITCD/TSB/Misc 52 (Oct. 7, 1999), at <http://www.unctad.org/en/docs/poitcdtsbm52.en.pdf>.

<sup>132</sup> EC Council Regulation, *supra* note 120, arts. 15(1) & 22(1). See also Bartels, *supra* note 15, at 509.

<sup>133</sup> EC Council Regulation, *supra* note 120, arts. 15(2) & 22(2).

<sup>134</sup> Steve Charnovitz has pointed out that the incentive preferences for drug-fighting countries were not really conditional because Europe did not specify the basis for providing the special preferences. See Howse et al., *Internet Roundtable*, *supra* note 12, at 239. Although his factual statement is accurate, our view is that these preferences should be viewed as conditional under conditions that were never revealed. There was some basis for awarding these preferences, even if it was a secret or impermissible reason.

<sup>135</sup> EC Council Regulation, *supra* note 120, art. 10 (referring to Column I of Annex I for a list of the beneficiary countries). In fact, although the Appellate Body did not mention it, Pakistan was added to the list of beneficiary countries soon after the terrorist attacks against the United States on September 11, 2001. See, e.g., *Indian Wins GSP Case Against European Commission at the WTO*, FIEO News, (Jan. 2004) at <http://www.fieo.org/fieonews/2004/january/wto.html>. This was widely seen as a way to



the Andean Community, the Central American States and Pakistan,<sup>136</sup> which gave a competitive advantage to producers from those countries. Accordingly, although all developing countries were given duty free access on non-sensitive products, only the twelve Drug Arrangement countries were given duty free access on sensitive products.<sup>137</sup> Moreover, Europe included some products in the Drug Arrangement that were not included in the General Arrangement,<sup>138</sup> on those products, the non-Drug Arrangement countries would have to pay the full tariffs, while the Drug Arrangement countries would pay no tariff. The selectivity of the Drug Arrangement had long been controversial among the developing countries,<sup>139</sup> and it became the focus of India's challenge.<sup>140</sup>

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reward Pakistan for its cooperation in the subsequent attacks by the United States British coalition on the terrorists in Afghanistan. *Id.*

<sup>136</sup> Under Column I of Annex I, the European Commission designated Bolivia, Colombia, Costa Rica, Ecuador, Guatemala, Honduras, Nicaragua, Panama, Peru, Pakistan, El Salvador and Venezuela as the beneficiary countries of the special arrangements for drug production and trafficking. EC Council Regulation, *supra* note 120, Annex I, Col. I.

<sup>137</sup> *Id.* art. 7.1-7.2.

<sup>138</sup> *Id.* art. 8-10.

<sup>139</sup> In fact, the European Union's earlier programs of trade concessions for combating drug production had been the target of two complaints at the WTO. Daniel Pruzin, *India Seeks WTO Talks with EU over Labor, Drugs Clauses in GSP Program*, 19 INT'L TRADE REP. 456 (2002). In October 2000, Brazil complained about EU tariff concessions on soluble coffee imported from several of its South American neighbors because of their efforts to combat drugs, while at the same time "graduating" Brazil's coffee exports from the GSP scheme. *Id.* This dispute was later resolved through a bilateral deal giving Brazil duty-free access for up to 10,000 metric tons of soluble coffee exports to the EU. *Id.* In December 2001, Thailand requested WTO consultations with the EU to address its complaint regarding unfair treatment of its exports arising from the special tariff arrangement for drugs. *Id.* Thailand's complaint is similar to India's because it is also excluded from the tariff arrangement even though it is doing as much or even more than the beneficiary countries in fighting illegal drugs. *Id.*

<sup>140</sup> India initially challenged each of the conditional features of the EC program, but, during consultations, dropped its broad attack and focused its arguments on the additional preferences that were connected with drug programs. *European Communities – Conditions for the Granting of Tariff Preferences to Developing Countries - Report of the Panel*, at 1, ¶1.5, WT/DS246/R (Dec. 1, 2003) [hereinafter *EC-Conditional Preferences*, Panel Report]. This is not a concession by India that the special arrangements for environmental and labor rights are beyond challenge. *Id.* As India noted in its decision to drop those claims, no preferences had been granted under the special incentive arrangements for the protection of the environment and only one

### B. The Decision

The Appellate Body's ruling on this challenge is quite narrow, dealing only with the issue of whether Europe violated the requirement of "non-discrimination" in GSP programs by granting Pakistan, but not India, special privileges under its drug program.<sup>141</sup> As one commentator has noted, because the special drug preferences were "only available to a 'closed list' of twelve beneficiaries," without an administrative procedure for recognizing new beneficiary countries, and without stated criteria for awarding the special preferences, the European plan was an "easy target."<sup>142</sup> Nonetheless, the methodology used by the Appellate Body is worth studying in some detail because such study reveals the Appellate Body's broader views about the legal implications of conditional GSP programs.

The Appellate Body first held that, in order to qualify for an exception to the MFN obligation under the Enabling Clause, the preferences had to be given on a general, non-discriminatory, and non-reciprocal basis.<sup>143</sup> This holding was itself not obvious.<sup>144</sup> Although the evidence is clear that, as originally envisioned, the GSP Preferences were intended to meet this standard,<sup>145</sup> the

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country, Moldova, had been accorded preferences under the incentive arrangements for the protection of labor rights. *Id.* India reserved its right to bring separate new complaints on the environmental and labor arrangements if the European Communities were to apply them in a manner detrimental to India's trade interests or if the European Communities were to renew them after the lapse of its current General System of Preferences Scheme on December 31, 2004. *Id.*

<sup>141</sup> AB REPORT, *supra* note 4, ¶190.

<sup>142</sup> Howse et al., *Internet Roundtable*, *supra* note 12, at 241-42.

<sup>143</sup> AB REPORT, *supra* note 4, ¶147.

<sup>144</sup> Robert Howse, for example, mounted a sustained attack on the notion that the Enabling Clause required GSP preferences to be "general, non-discriminatory, and non-reciprocal." See Howse, *India's WTO Challenge*, *supra* note 12, at 388-393 (arguing that the key language of the Enabling Clause does not create a legally enforceable standard). His position was softened, but still critical, after the Appellate Body ruled to the contrary. See Howse et al., *Internet Roundtable*, *supra* note 12, at 246 (arguing that Appellate Body should have supported its analysis with reference to the object and purpose of the Enabling Clause).

<sup>145</sup> The Preamble to the 1971 GSP Decision clearly confirms, as was contemplated in both the First and Second UNCTAD Reports that "unanimous agreement was reached in favor of the early establishment of a mutually acceptable system of *generalized, non-reciprocal, non-discriminatory* preferences, beneficial to developing countries . . ." 1971 Waiver, *supra* note 62, Preamble.

Enabling Clause itself did not make this standard clear. This standard was mentioned only in footnote 3 of the Enabling Clause, which provided that the preferences would be those “[a]s described in the decision of 1971 relating to the establishment of the general, non-reciprocal, and non-discriminatory system.”<sup>146</sup> The Appellate Body wisely ruled that this was not merely a descriptive reference to the original program, but instead incorporated the substantive requirements of the program as originally approved.<sup>147</sup>

Having found that the GSP Program must be “general, non-reciprocal, and non-discriminatory” in order to qualify for the exemption from the Article I MFN requirement, the Appellate Body went on to discuss and apply the requirement that GSP programs be “non-discriminatory” as between the potential recipients of the programs.<sup>148</sup> The Appellate Body set forth two general principles. First, it made it clear that “non-discriminatory” does *not* mean that no distinctions can be drawn between the programs offered to various countries;<sup>149</sup> second, it determined that *similarly situated countries must be treated similarly*.<sup>150</sup> Formally equal treatment among developing countries is not required, and a granting country may group countries into categories that have different characteristics, but similar countries must be dealt with

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<sup>146</sup> Enabling Clause, *supra* note 63, at n.3.

<sup>147</sup> AB REPORT, *supra* note 4, ¶¶146-47.

<sup>148</sup> *Id.*

<sup>149</sup> AB REPORT, *supra* note 4, ¶156 (stating “it does not necessarily follow, however, that ‘non-discriminatory’ should be interpreted to require that preference-granting countries provide ‘identical’ tariff preferences under GSP schemes to ‘all’ developing countries”).

<sup>150</sup> *Id.* ¶154 (stating that “[i]t is clear from the ordinary meaning of ‘non-discriminatory,’ however, that preference granting countries must make available identical tariff preferences to all similarly-situated beneficiaries”); *see also* ¶173 which states:

We conclude that the term ‘non-discriminatory’ in footnote 3 does not prohibit developed country Members from granting different tariffs to products originating in different GSP beneficiaries . . . . 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 . . . .

*Id.*

similarly.<sup>151</sup>

The reason for this interpretation is straightforward. As the Appellate Body recognized in its earlier *Shrimp-Turtle* decision,<sup>152</sup> the equal treatment of countries that are not the same can be discriminatory.<sup>153</sup> To treat different countries equally it is necessary not only to avoid formal discrimination but also to take into account the different circumstances that make formally equal treatment damaging to a country.<sup>154</sup> So the restriction on non-

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<sup>151</sup> The Appellate Body cited sources in general international law for these propositions. *See id.* ¶153, n. 318.

<sup>152</sup> *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, Report of the Appellate Body, WT/DS58/AB/R (Nov. 6, 1998) [hereinafter *US-Shrimp*]; *see also United States—Section 337 of The Tariff Act of 1930*, 36th Supp. BISD 3454 (1990) (stating that under national treatment discrimination, formal equal treatment can be discriminatory while differential treatment can be lawful if it is not unfavorable treatment).

<sup>153</sup> Indeed, this is the basis for the GSP program in the first place—the recognition that treating poor countries the same as rich countries would in fact discriminate against the poor countries. *See generally* Yusuf, *supra* note 16, at 492 (noting that the principle of equality does not impose a legal obligation on States to treat all other States equally in those areas where rights and duties are regulated on the basis of contractual obligations, and therefore discrimination or differential treatment of other states in matters of trade was not unusual) *Id.* Yusuf believes the only way to assure non-discriminatory treatment lies in the negotiations of treaties, such as GATT, that were based on the MFN Clause. *Id.* at 492. On the other hand, Professor Regan is “surprised and dismayed by the ease with which academics say that ‘discrimination’ includes . . . similar treatment of entities differently situated.” *See* Howse et al., *Internet Roundtable*, *supra* note 12, at 263. His objection, however, appears to be institutional rather than jurisprudential. He states that although the notion “might make sense in some idealized world . . . in the actual world. . . [the statement] is much more troublesome.” *Id.* The Appellate Body’s continued reference to the principle reflects their view that formal equality is too relaxed a principle in a world where inequality is rife, and they draw on well-recognized authority for the proposition. *See* AB Report, *supra* note 4, at ¶153, n. 318. Perhaps Professor Regan’s concern might be alleviated if we recognize that the Appellate Body does not seem intent on requiring positive changes in law; they do not require, for example, that a country affirmatively give greater preferences to poorer countries. *Id.* Rather, they seem to be contemplating that when a country seeks to deal with a problem like drug enforcement or nearly extinct species, it does so by taking into account not only the extent to which the problem is the same in various countries but also the extent to which the problem is different in different countries. *Id.*

<sup>154</sup> *See US-Shrimp*, *supra* note 152, at ¶164 (stating that “it is not acceptable in international trade relations for one WTO Member to use an economic embargo to require other Members to adopt essentially the same comprehensive regulatory program, to achieve a certain policy goal, as that in force within that Member’s territory without taking into consideration different conditions which may occur in the territories of those

discrimination cannot be a requirement of formally equal treatment; it must be a requirement that the granting country treat equal countries equally and unequal countries unequally.

This standard of non-discrimination, however, requires us to understand which characteristics of a country matter when we determine whether countries are similarly situated. If, for example, a GSP donor country may consider a country's political system when deciding what preferential treatment to give, it could have one preference system for functioning democracies and another preference system for oligarchic democracies. If the granting country were allowed to take religion into account, then it could have one preference system for Islamic countries and another for Christian countries. The discrimination standard requires that the basis for treating countries differently be specified.

When the Appellate Body looked to see what criteria a donor country may use to determine whether it could, or must, treat countries differently, it saw that the standard was contained within the Enabling Clause itself.<sup>155</sup> According to the Enabling Clause, the preferences are to be "designed and, if necessary, modified, to respond positively to the development, financial and trade needs of the developing countries."<sup>156</sup> This is the standard that determines the basis for differentiating between the preferences given to particular countries—the classification must bear some relationship to the different developmental, financial and trade needs of different classes of countries.<sup>157</sup> Under this standard, a

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other Members") and ¶165 (stating that "we 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 any inquiry into the appropriateness of the regulatory program for the conditions prevailing in those exporting countries").

<sup>155</sup> See AB Report, *supra* note 4, ¶165.

<sup>156</sup> Enabling Clause, *supra* note 63, ¶3(c).

<sup>157</sup> The development emphasis of the Enabling Clause is apparent in other provisions as well. For example, Paragraph 9 of the Enabling Clause calls for a review of its provisions "bearing in mind" the need "to meet the development needs of developing countries." *Id.* ¶9. This is, of course, consistent with the program that was originally created through negotiations at UNCTAD. *Agreed Conclusions of the Special Committee on Preferences*, UNCTAD Doc. TD/B/330, part II. The *Agreed Conclusions of the Special Committee on Preferences* stipulated that the preferences would be exclusively for developing states and territories and that no non-developing third country

preference system that distinguishes between countries on the basis of their form of government or their religion would be sustained as “non-discriminatory” only if it could be shown that the form of government or religion had some relationship to the developmental, financial or trade needs of the country.<sup>158</sup>

As the Appellate Body said, “the expectation that developed countries will ‘respond positively’ to the ‘needs of developing countries’ suggests that a sufficient nexus should exist between, on the one hand, the preferential treatment provided under the respective measure authorized [by the Enabling Clause] and, on the other, the likelihood of alleviating the relevant ‘development, financial, [or] trade need.’”<sup>159</sup> Accordingly, different preferences for different countries are permissible if the donor country classifies recipients according to their different developmental, financial or trade needs.

Applying this standard in *EC—Conditional Preferences* might have led the Appellate Body to evaluate Europe’s basis for classifying some countries as especially worthy of receiving preferences because of their drug fighting programs, while finding other countries unworthy under that criterion. Arguably, the Appellate Body could have examined the relationship between programs for fighting drugs and the development, financial, and trade needs of developing countries, and then could have asked whether Pakistan’s anti-drug programs were really better (along some relevant measure) than those of India. However, because the panel from which the appeal was taken had made no findings on these subjects,<sup>160</sup> and neither party had raised this issue, the Appellate Body decided the case on the assumption that a donor country can give different levels of preferences to countries that effectively fight drug traffic.<sup>161</sup>

The Appellate Body nonetheless struck down Europe’s preference program as applied because it did not offer sufficient procedural assurances that the program would be applied non-

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was to invoke its rights to MFN treatment with a view towards obtaining these same preferences. *Id.*

<sup>158</sup> AB REPORT, *supra* note 4, ¶166.

<sup>159</sup> *Id.* ¶165.

<sup>160</sup> *Id.* ¶130.

<sup>161</sup> *Id.*

discriminatorily.<sup>162</sup> Here, the Appellate Body drew on a judicial technique reminiscent of the one it used in the *Shrimp-Turtle* decision, by setting up a series of procedural hurdles that any GSP donor country must face before it can sustain its differential treatment between countries based on their developmental, financial and trade needs.<sup>163</sup> Because the conditional privileges that Europe gave, “may be found consistent with the ‘non-discriminatory’ requirement in footnote 3 only if the European Community proves, at a minimum, that the preferences granted under the Drug Arrangement are available to all GSP beneficiaries that are similarly affected by the drug problem,”<sup>164</sup> Europe also had to adopt practices that would ensure that it met that standard.

First, Europe had to provide a mechanism for adding to the list of beneficiary countries; for, without such a mechanism, there would be no way for countries that came into compliance with the conditions to show that they too were entitled to the extra privileges.<sup>165</sup> Europe had provided such a mechanism with respect to its special incentives for labor and environmental standards, but not with respect to the drug standards.<sup>166</sup> In particular, Europe “gives no indication of how the beneficiaries under the Drug Arrangement were chosen or what kind of considerations would or could be used to determine the effect of the ‘drug problem’ on a particular country [and no] indication as to how the European Communities would assess whether the Drug Arrangements provide an ‘adequate and proportional response’ to the needs of developing countries suffering from the drug problem.”<sup>167</sup> Accordingly, its program was discriminatory within the meaning of the Enabling Clause.

Second, Europe had not set any clear prerequisites or objective criteria that would guide the determination of which countries are within the similarly situated class.<sup>168</sup> Without such a set of

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<sup>162</sup> *Id.* ¶¶187-88.

<sup>163</sup> *Id.*

<sup>164</sup> AB REPORT, *supra* note 4, ¶180.

<sup>165</sup> *Id.* ¶182.

<sup>166</sup> *Id.*

<sup>167</sup> *Id.* The reference to “adequate and proportional response” is from one of the submissions made in the case by the European Community. *Id.* n. 386.

<sup>168</sup> *Id.* ¶183. The Appellate Body had earlier stated that “broad-based recognition of

criteria, developing countries would be unable to determine whether they should seek to be qualified for the privileges, and dispute panels charged with reviewing the preference conditions would have no way of determining whether the donor countries' decisions were based on development, financial, or trade needs of the potential recipients.

Finally, just as there were no criteria for adding a country to the list of special beneficiaries, there were no criteria for removing a country.<sup>169</sup> This too could result in discrimination, for continuing preferences for a country that does not deserve them under the relevant standard would be as discriminatory as denying them to a country that does.

In short, the European system "itself gives no indication as to how the beneficiaries under the Drug Arrangements were chosen or what kind of considerations would or could be used to determine the effect of the 'drug problem' in a particular country."<sup>170</sup> The lesson of the case is clear: when a developed country exercises its power, it must follow procedures that help to ensure that it is not abusing its power. Requiring these procedures is necessarily a reflection of the fact that determining conditions on which preferences will be granted directly affects the welfare of these developing countries. In order to guarantee that these decisions are not discriminatory, the donor must provide objective standards and follow procedural mechanisms in making their decision.

## V. Legal Implications for Other Conditional GSP Programs

Although the Appellate Body's holding in *EC – Conditional Preferences* was quite narrow, the Appellate Body revealed a methodology that allows us to understand how they will likely analyze future challenges to conditions placed on GSP programs. We set forth this understanding in this section, providing an analytical framework for assessing which conditions are likely to be upheld and which are likely to be overturned. This legal analysis does not, however, provide a complete understanding of

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a particular need, set out in the *WTO Agreement* or in multilateral instruments adopted by international organizations, could serve as such a standard." *Id.* ¶163.

<sup>169</sup> *Id.* ¶183.

<sup>170</sup> AB REPORT, *supra* note 4, ¶183.



how the Appellate Body is likely to act in future cases, because conditional GSP programs present the Appellate Body with political, as well as legal, challenges. Accordingly, in the next section of the article, we explain how our analysis of the law affecting conditional GSP programs also puts the Appellate Body in a position to monitor power relationships between countries and enhance developing country participation in the international trading system.

The three requirements of GSP programs – to be “general, non-discriminatory, and non-reciprocal” – are closely aligned with one another.<sup>171</sup> In particular, each is likely to be understood in light of the two major interpretive messages of the *EC-Conditional Preferences* case: First, that the conditions under which GSP benefits are to be given must relate to the circumstances of the recipient countries, not the circumstances or welfare of the granting country; and, second, that the terms are to be construed in light of the provisions of the Enabling Clause that restrict and shape GSP programs.<sup>172</sup> Although we take up each of the three terms separately, we do it in a manner that demonstrates how they are interconnected.

#### A. Interpretation of the Term “General”

The terms “general” and “non-discriminatory” largely overlap, because the former term is a subset of the latter. As the Appellate Body explained, preferences must be general in the sense that they may not be confined to a subset of developing countries that have a particular historical, cultural, political or geographic relationship with the granting country.<sup>173</sup> Accordingly, the preferences that some European countries had with their former colonies are ineligible for the MFN exemption under the Enabling Clause.<sup>174</sup> This provision constitutes a subset of the general prohibition against discriminatory preferences because it states that the preference programs may not set up classifications that discriminate among recipients on any of these circumstance that would make the benefits special—that is, based on historical,

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<sup>171</sup> Enabling Clause, *supra* note 63.

<sup>172</sup> AB REPORT, *supra* note 4.

<sup>173</sup> *Id.* ¶155.

<sup>174</sup> Yusuf, *supra* note 16, at 488.

cultural, political or geographic relationships—rather than general.<sup>175</sup> Such ties are not a permissible basis for discriminating in favor of, or against, recipient countries.

Naturally, issues of proof remain. The identification of classifications that relate to these special considerations appears not to be difficult, for they are all capable of identification using the normal methods of proof. Classifications that appear on their face to favor countries because of these relationships undoubtedly will be struck down as *de jure* discrimination.<sup>176</sup> In addition, complaining countries will also be able to prevail if they can prove, from the way that the classifications apply in practice, that facially neutral classifications nonetheless amount to *de facto* discrimination on one of the impermissible criteria.<sup>177</sup> This analysis will draw on well-understood tests under WTO law for challenging *de facto* conditions.<sup>178</sup>

### B. Interpretation of the Term “Non-Discriminatory”

Provided that the classification used by the donor country does not discriminate on the basis of historical, cultural or geographic relationships, the Appellate Body must then determine if other grounds are permitted for classifying some developing countries as privileged beneficiaries—that is, for making benefits conditional on inclusion within the privileged group. Several grounds for permissible discrimination are clear. First, donor countries may discriminate based on a country’s level of development; Europe’s special privileges for least developed countries seem to be beyond reproach because the Enabling Clause explicitly permits special

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<sup>175</sup> *Id.*

<sup>176</sup> See generally Appellate Body Report, Canada—Measures Affecting The Export of Civilian Aircraft—Recourse by Brazil to Article 21.5 of the DSU, WT/DS70/AB/RW, (Aug. 4, 2000) (setting forth method for determining whether subsidies are contingent on exporting); Thailand—Restrictions on Importation of and Internal Taxes on Cigarettes, GATT B.I.S.D. (37th Supp.) at 204 (Nov. 7, 1990) (reviewing Thai regulations of cigarettes that were non-discriminatory on their face but discriminatory as applied); Japan—Taxes on Alcoholic Beverages, WT/DS8-11/AB/R, (Nov. 1, 1996) (determining whether *de jure* non-discriminatory tax was nonetheless *de facto* discriminatory because it was applied “so as to afford protection”).

<sup>177</sup> Yusuf, *supra* note 16.

<sup>178</sup> *Id.*

benefits for least developed countries.<sup>179</sup>

Moreover, the Enabling Clause also suggests that as countries develop, they can be asked to take on more and more conditions.<sup>180</sup> This implies that donor countries may classify recipient countries by level of development and, accordingly, grant different levels of privileges. This is inherent in the graduation clause in paragraph 7 of the Enabling Clause, which explicitly provides that:

Less-developed contracting parties expect that their capacity to make contributions or negotiated concessions or take other *mutually agreed action* under the provisions and procedures of the General Agreement would improve with the progressive development of their economies and improvement in their trade situation and they would accordingly expect to participate more fully in the framework of rights and obligations under the General Agreement.<sup>181</sup>

Although this graduation clause suggests that recipient countries may be treated differently on the basis of their level of development, this is not unlimited permission to increase conditions as a country becomes wealthier. This permission for donor countries to discriminate on the basis of the level of development explicitly depends on conditions being “mutually agreed” upon.<sup>182</sup> At a minimum, this will put the Appellate Body in the position of determining whether the granting country has bargained in good faith with the recipient country to ensure that the heightened conditions actually reflect the improvement in the economic and trade position of the recipient countries and are not

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<sup>179</sup> Enabling Clause, *supra* note 63, ¶2(d) (authorizing donor countries to grant special benefits to least developed developing countries).

<sup>180</sup> *Id.*

<sup>181</sup> *Id.* ¶7 (emphasis added). The 1982 Secretary-General of UNCTAD, however, in his assessment of the results of the Multilateral Trade Negotiations, noted some apprehension regarding the graduation clause because although it was “vaguely worded,” it establishes a legal precedent within the GATT system by requiring the developing countries to accept greater obligations as their economic situation improves. 1982 Report by the Secretary General of the UNCTAD, *Assessment of the Results of the Multilateral Trade Negotiations*, UNCTAD Doc. T/B/778/Rev.1, at 29, ¶179. Moreover, the report also foresaw that this graduation concept could have far-reaching consequences for the future WTO system if its implementation were to allow developed countries to discriminate among developing countries in a unilateral and arbitrary manner. *Id.*

<sup>182</sup> AB REPORT, *supra* note 4, at 81.

inconsistent with the continuing developmental, financial, and trade circumstances of the country.

Aside from permissible discrimination based on a country's level of development, no *a priori* judgments can be made regarding which bases of discrimination are consistent with the requirements of the Enabling Clause. Whether a donor country can discriminate on the basis of the labor or environmental policy of a recipient country, for example, must be left to case-by-case adjudication.<sup>183</sup> Several principles, however, are likely to guide the Appellate Body in this inquiry.

First, it is unlikely that the Appellate Body will accept generalized statements that link a country's differential treatment to development conditions in the recipient countries. As the Appellate Body said, "need cannot be characterized . . . based merely on an assertion to that effect;" rather, the donor country must refer to "[b]road based recognition of a particular need, set out in the *WTO Agreement* or in multilateral instruments adopted by international organizations"<sup>184</sup> In other words, the Appellate Body is unlikely to accept the general argument that fighting drug traffic is good for a country or for international trade. Instead, it is likely to insist that the donor country shows with some specificity the relationship between the conditions that the recipient countries must meet, and the development, financial and trade needs of the country. This notion is reinforced by the requirement, read by the Appellate Body into the Enabling Clause, that the granting country must rely upon "objective criteria" when determining whether an applicant country is entitled to receive benefits.<sup>185</sup>

Moreover, the Appellate Body may review the connection between the policies that donor countries require and the development, financial, and trade needs of recipient countries. As the Appellate Body said,

[A] sufficient nexus should exist between, on the one hand, the preferential treatment provided under the respective

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<sup>183</sup> *Id.* at 12.

<sup>184</sup> AB REPORT, *supra* note 4. In a footnote to that paragraph, the Appellate Body noted that the EC finds support "in several international conventions and resolutions that have recognized drug production and drug trafficking as entailing particular problems for developing countries." *Id.* n. 335.

<sup>185</sup> *Id.* ¶ 183.

treatment . . . and, on the other, the likelihood of alleviating the relevant “development, financial [or] trade need.” In the context of a GSP scheme, the particular need at issue must, by its nature be such that it can be effectively addressed through tariff preferences.<sup>186</sup>

Indeed, the purpose of specifying the relationship between the conditions and the developing need of the recipient country must be to allow this nexus to be evaluated.

Undoubtedly, this inquiry into the relationship between the donor’s conditions and the development interest of the recipient country will require the Appellate Body to undertake a difficult analysis to determine which policies stimulate growth and which policies do not. One can imagine that a scheme that conditioned benefits on the recipient country having a certain kind of intellectual property regime, for example, is likely to be contentious, since the link between intellectual property and growth is itself contentious.<sup>187</sup> On the other hand, conditions that require the recipient country to follow well-developed policies for sustainable development or worker health and safety are likely to be given presumptive weight by the Appellate Body.<sup>188</sup> In these considerations, the Appellate Body is likely to be swayed not only by the reigning ideology of developmental economics, but also by any developmental plan that the recipient country has in place. Conditions that reflect the plans drawn up by developing countries are more likely to be seen as in that country’s interest than are plans that are created by the granting country.

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<sup>186</sup> *Id.* ¶ 164.

<sup>187</sup> *Compare* REPORT OF THE COMM’N ON INTELLECTUAL PROP. RIGHTS, INTEGRATING INTELLECTUAL PROP. RIGHTS & DEV. POLICY (2002), available at <http://www.iprcommission.org/graphic/documents/final-report.htm> (expressing skepticism about the contribution of intellectual property to development and arguing that developing countries should carefully tailor their intellectual property systems to their development needs) with ROBERT M. SHERWOOD, INTELLECTUAL PROPERTY AND ECONOMIC DEVELOPMENT (1990) (claiming that intellectual property is good for development because it attracts foreign investment and technology transfer). The evidence is collected and reviewed in KEITH MASJUS, INTELLECTUAL PROPERTY RIGHTS IN THE GLOBAL ECONOMY (2002).

<sup>188</sup> See Bartels, *supra* note 15, at 652 (stating that conditioning preferences on standards that are already binding on developing countries can be the basis for GSP conditions, but insistence on non-binding standards that the developing country does not have the technical or economic capacity to meet will be impermissible).

As a second general principle, it is likely that the Appellate Body will more easily uphold conditions if the recipient country is required to expend resources to meet the conditions, and if the preferences are designed to compensate the recipient country for those expenditures. Some programs that are good for a country in the long term, such as environmental and labor protections, are nonetheless expensive to finance in the short term. Preference programs that are designed to compensate a country for those expenses would be in the interests of the recipient country, and would therefore meet the applicable standard (even if conditioning general preferences on labor and environmental rights alone would not). Accordingly, preferences that serve as carrots to allow the recipient country to offset the cost of policy that is good for the country in the long run will probably be upheld.

For this reason, the Appellate Body is likely to approve extra preferences that go beyond those generally available for countries in a certain class if the extra benefits offset obligations that the recipient country is undertaking in order to advance its own development. Even here, however, the Appellate Body is likely to police closely the conditions on which the extra privileges are given in order to make sure that the value of the extra privileges is comparable to the burdens that the recipient country is undertaking. Privileges that are small in relation to the cost to the recipient country, and that require conditions that reduce the financial, trade, and/or development position of the recipient country are not likely to be allowed.

Third, the Appellate Body is likely to uphold conditions that seek to insure that the benefits of preferential treatment are actually translated into benefits for the people of the country, and that they are not siphoned off into wasteful or corrupt practices.<sup>189</sup> No donor country should be required to grant preferential benefits unless it has some assurance that the money is used for the purpose for which it was given.<sup>190</sup>

### *C. Requirement of "Non-reciprocal"*

Reciprocity among the WTO members is a foundational

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<sup>189</sup> See *supra* Part III.

<sup>190</sup> *Id.*

principle of the WTO regime.<sup>191</sup> The stipulation that benefits be non-reciprocal is a reflection of the special nature of the exception that is granted to the MFN requirement—the central expression of the notion that GSP programs are gifts, not exchanges.<sup>192</sup> The recipient country may not be required to give anything of value to the granting country as a condition of receiving the benefits.<sup>193</sup> Placing conditions on the receipt of privileges is permissible as long as they benefit the recipient country and not the donor country; if the recipient country is not giving anything of value to the donor country, the privileges are then non-reciprocal.<sup>194</sup>

At a minimum, the requirement of non-reciprocity means that the granting country may not require the recipient country to lower tariff or non-tariff barriers in order to get benefits. The GSP program is expected to exist outside of the normal exchange of market access concessions. In fact, no GSP program that we know of conditions the benefits on giving the granting country market access.

However, the requirement of non-reciprocity extends further. The GATT/WTO system has long followed the practice of requiring reciprocity in all of its commitments; that is the essence of the “single undertaking” that requires WTO members to subscribe to all the obligations that are contained in multilateral agreements.<sup>195</sup> To limit the requirement of non-reciprocity to trade-like concessions would allow the granting country to exact other promises of value to the granting country that would make the benefits costly. Any condition that requires the recipient country to do something that is not in its interests in order to

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<sup>191</sup> See, e.g., HUDEC, *supra* note 52, at 4 (noting a history “based essentially on parity of obligation”); see generally PATRICK LOW, *TRADING FREE: THE GATT AND U.S. TRADE POLICY* 29 (1993) (discussing notions of fair trade and reciprocity, why they are sought through GATT tariff negotiations, and the difficulties these goals present); Michael K. Young, *Lessons From the Battle Front: U.S.-Japan Trade Wars and Their Impact on the Multilateral Trading System*, 33 *GEO. WASH. INT’L L. REV.* 735, 762 (2001) (exploring facets of the right to seek reciprocal trade concessions).

<sup>192</sup> Enabling Clause, *supra* note 63, ¶ 5.

<sup>193</sup> *Id.*

<sup>194</sup> *Id.*

<sup>195</sup> See generally LOW, *supra* note 191 (discussing notions of fair trade and reciprocity, why they are sought through GATT tariff negotiations, and the difficulties these goals present).

“compensate” the granting country for giving the preferences makes the benefits non-reciprocal.

This reading is not only drawn from the logic of the Appellate Body opinion in *EC—Conditional Preferences*, but is also confirmed by the negotiating history of the GSP system itself. For example, the first UNCTAD Report said that “developed countries . . . *should not, in granting these or other [trade] concessions, require any concession in return from developing countries.*”<sup>196</sup> This broad view of non-reciprocity—the prohibition on developed countries requiring any concessions—was then incorporated into Paragraph 5 of the Enabling Clause, which provides that “the developed countries do not expect the developing countries, in the course of trade negotiations to make contributions which are inconsistent with their individual development, financial, and trade needs.”<sup>197</sup>

This, of course, will require the Appellate Body to engage in the same kind of analytical question about the impact of the conditions on the recipient country that it undertakes when it determines whether the basis on which the granting country differentiates between developing countries is acceptable.

Given this analysis, we can discern the framework for

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<sup>196</sup> Principle 8 of Recommendation A.I.1 in *Final Act of the First United Nations Conference on Trade and Development* (Geneva: UNCTAD, Doc E/COMF.46/141, 1964), Vol. 1 at 20 (emphasis added). The Generalized System of Preferences originated in 1964 at the first UNCTAD, and the Conference, although recognizing that international trade should be conducted to the mutual advantage of Member States on the basis of most-favored nation treatment, nevertheless settled upon this non-reciprocity principle. *Id.* Likewise, at the second UNCTAD, this commitment to non-reciprocity by developing countries was once again recognized in Resolution 21(II)'s Agreed Conclusions. The Agreed Conclusions recognized “the unanimous agreement in favor of the early establishment of a mutually acceptable system of generalized, non-reciprocal, non-discriminatory preferences which would be beneficial to developing countries.” *Agreed Conclusions of the Special Committee on Preferences*, UNCTAD Doc. TD/B/330, part II.

<sup>197</sup> Enabling Clause, *supra* note 63, ¶ 5 (emphasis added). Although this section of the Enabling Clause expresses an expectation rather than a legal requirement, because the expectation refers to the nature of the reciprocity that is expected in GSP programs, it is an appropriate indication of the meaning of the term “non-reciprocal.” *Id.* Further, this same paragraph of the Enabling Clause requires then that developed Contracting Parties “shall not seek, neither shall less-developed countries be required to make, concessions that are inconsistent with the latter’s development, financial and trade needs.” *Id.*



analyzing conditions that granting countries impose on developing countries before they can get preferential treatment. The conditions must be non-discriminatory in that they classify countries on the basis of their developmental, financial, and trade needs and treat equally situated countries equally. They must also ensure that the conditions that serve as a prerequisite for the preferences are tailored to help the developing country meet these specific needs. Under this framework, the Appellate Body is likely to uphold positive conditionality<sup>198</sup> (i.e. “extra” preferences that are designed to finance developing country investment in certain policy changes) when those preferences can be seen as compensation for the country undertaking the required policy changes. Positive conditions are less likely to impose a cost on the recipient country, and they ensure that the donor country pays for any benefit that it gets from the recipient country’s change in policy.<sup>199</sup> Negative conditionality, the condition of any preferences on changes in policy,<sup>200</sup> is likely to be more problematic unless there is an objective relationship between the conditions required for getting the preferences and the needs of the GSP program (such as country of origin requirements) or the development, financial, and trade needs of the developing country.

Even within this general framework, however, the Appellate Body has large interpretive flexibility. For example, what burden will a donor country have to demonstrate that the conditions it imposes meet the development, financial, and trade needs of the recipient countries? How are those conditions distinguished from conditions that require the recipient country to give something of value to the donor country that is not in their interest? Even aside from these questions, the Appellate Body must determine whether the donor country has met the kind of procedural hurdles that are an intricate requirement of the ability to impose conditions or classifications on recipients: the requirement that the donor country articulate the standards to be employed, that it specify the relationship between the conditions and the interests of the

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<sup>198</sup> See *supra* note 47 and accompanying text.

<sup>199</sup> Other commentators agree with this assessment. See Howse et al., *Internet Roundtable*, *supra* note 12, at 240, 245 (concluding that positive conditionality is likely to face fewer hurdles than negative conditionality).

<sup>200</sup> See *supra* note 88 and accompanying text.

recipient country, that it provide procedures by which recipient countries can show that they qualify for the special privileges, and that it engage in good faith discussions about the relationship between the conditions it imposes and the ends that it is allowed to pursue.<sup>201</sup>

For these reasons, the Appellate Body has a great deal of interpretive space; it can apply the framework one way or the other, increase burdens of proof, heighten or lower the procedural hurdles, or impose even more stringent controls on the ways in which donor countries use conditional preferences. It is relevant, therefore, to develop a sense of the ways in which the Appellate Body is likely to use its interpretive freedom on a case-by-case basis.

## VI. The Role of the WTO Appellate Body

The Appellate Body has proven to be deliberative and systematic in its interpretive work in an important and creative way: the Appellate Body situates its interpretive task in the context of the WTO regime as a whole, and in terms of the relationship between the WTO system and other manifestations of international law.<sup>202</sup> Within the WTO context, the Appellate Body is consciously creating a jurisprudence of treaty interpretation that relies on a consistent set of analytical techniques for matching means and ends and for understanding the relationship between various treaty provisions. In addition, the Appellate Body is conscious of the relationship between the WTO regime and the other international law regimes with which the WTO must interact.<sup>203</sup> Although adhering in name to the Vienna Convention on the Interpretation of Treaties, the Appellate Body has found enough flexibility in that document to allow it to think

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<sup>201</sup> See AB REPORT, *supra* note 4.

<sup>202</sup> This is evident in the opinion in *EC—Conditional Preferences* itself. As one commentator has said, “the most striking feature of this AB report is how ambitious and self-confident it is laid out.” Howse et al., *Internet Roundtable*, *supra* note 12, at 255. See also, Sol Picciotto, *The WTO’s Appellate Body Legal Formalism as a Legitimation of Global Governance*, 18 GOVERNANCE — (publication forthcoming, 2005) (acknowledging the Appellate Body’s formalism and reliance on legalisms, but suggesting that the Appellate Body could more forthrightly engage in policy discussions).

<sup>203</sup> Picciotto, *supra* note 202; Howse et al., *supra* note 12.

systemically while at the same time proceeding on a case-by-case basis.<sup>204</sup>

This creative and systemic deliberation is an essential characteristic given the nature of WTO lawmaking and the institutional environment in which the Appellate Body is embedded. Although the covered agreements are quite dense in some respects, their language is hardly self-applying and they contain numerous interpretive puzzles; not only are the treaty terms generally undefined, but the treaties also contain significant gaps.<sup>205</sup> Moreover, the decisions of the Appellate Body are not easily reversed, and therefore have a finality of almost constitutional import.<sup>206</sup> Despite provisions allowing for treaty amendments and waivers without consensus,<sup>207</sup> in practice members who want to reverse a decision of the Appellate Body must do so in the context of ongoing negotiations, which means that treaty amendment gets caught up in the time-consuming, intricate, and expensive work of treaty negotiation.<sup>208</sup> When judges interpret a statute, the legislative body that created the statute can review the interpretation and, normally, reverse it by a simple majority vote if the interpretation is inconsistent with Congressional intent (either originally or in light of the impact of the interpretation as it is applied).<sup>209</sup> To date, members of the

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<sup>204</sup> Picciotto, *supra* note 202; Howse et al., *supra* note 12.

<sup>205</sup> For example, the treaties are silent on the issue of what nexus one country must show between its interests and the environmental policy of another country before it imposes trade restraints to induce that country to change its environmental policies. Although the conventional assumption among trade experts was that one country had no legitimate interest in the processes by which other countries made products, that understanding was neither explicit in the treaties, nor inherent in the nature of the issues with which the treaties dealt. In *US-Shrimp*, the Appellate Body implicitly refused to apply the process/product distinction to preclude one country from expressing its interest in another country's process policies, thus exposing a gap in the scope of the treaties. *US-Shrimp*, *supra* note 152. Moreover, because of the political sensitivity of the nexus issue, the Appellate Body pointedly refused to answer the issue in the context of that case as well. *Id.*

<sup>206</sup> See generally WTO, *Understanding on Rules and Procedures*, *supra* note 2, art. 3.1.

<sup>207</sup> See Peter M. Gerhart, *Reflections: Beyond Compliance Theory – TRIPS as a Substantive Issue*, 32 CASE W. RES. J. INT'L L. 357, 382 (2000).

<sup>208</sup> *Id.*

<sup>209</sup> *Id.*

WTO have reversed none of the decisions of the Appellate Body through new negotiations.<sup>210</sup>

Further, the Appellate Body exercises compulsory jurisdiction and, unlike many national judicial bodies, has developed no "political question" jurisprudence that would allow it to refuse to make decisions on issues that are more properly considered political, rather than interpretive.<sup>211</sup> It has no way of avoiding the difficult issues that the members of the WTO have themselves refused, or been unable, to answer. Although it is sometimes asked to render decisions on quite technical legal issues, its decisions often present, and require, decisions on broad policy issues of great importance.<sup>212</sup>

Within this environment, the deliberate and systematic approach of the Appellate Body takes on special importance. Although the Appellate Body wields only interpretive power,<sup>213</sup> that power is significant, and is capable of both abuse and of positive impact. Should the Appellate Body exercise its interpretive powers without a sound appreciation for the systemic implications of its decisions, the Appellate Body would do great damage.<sup>214</sup> On the one hand, if the Appellate Body were to engage in too much creative lawmaking, it could easily upset the systemic balance that WTO members have sought to achieve. On the other hand, if the Appellate Body were to engage in too literal a reading of the terms of the treaty, without understanding the systemic needs of the WTO, the Appellate Body could risk destabilizing the system in a different direction.<sup>215</sup> The fact that the Appellate Body

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<sup>210</sup> *Id.*

<sup>211</sup> Some commentators have become concerned that the Appellate Body has no "political escape valve." See McRae, *supra* note 3, at 19.

<sup>212</sup> See Steven Charnovitz, *Judicial Independence in the World Trade Organization, International Organizations and International Dispute Settlement: Trends and Prospects* 231-232 (2002), available at <http://www.worldtradelaw.net/articles/charnovitzjudicial.pdf>.

<sup>213</sup> *Id.*

<sup>214</sup> Some commentators, in fact, are highly critical of the Appellate Body for usurping issues that are more properly the jurisdiction of the members, either collectively or individually. See generally John Ragosta, et al., *WTO Dispute Settlement: The System is Flawed and Must be Fixed*, 37 INT'L LAW 697 (2003) (suggesting that the Appellate Body leave more issues to individual or collective members).

<sup>215</sup> Given its own balancing act, it is not surprising that the Appellate Body is subject to criticism for being both too literal and too policy driven. See, e.g., McCrae,

makes deliberate and thoughtful decisions provides assurances that it is trying to avoid decisions that could do fundamental violence to the stability and functioning of the system.

Given the Appellate Body's deliberate approach to decision-making, and the systemic implications of its decisions, it is worthwhile to develop an understanding of which systemic characteristics are likely to have the greatest leverage on the Appellate Body. How should we think about the systemic values that seem to be at stake when the Appellate Body exercises its interpretive discretion?

Most commentators who have ventured an answer to this question have taken an institutional view of the role of the Appellate Body. Under one institutional perspective, the Appellate Body is allocating decision-making power among the various institutional actors that have a stake in the decision.<sup>216</sup> For example, the Appellate Body must allocate decision-making power among the various countries with interests in the subject matter, either restraining the power of one or unleashing the power of another, and must determine how much weight to give to the decisions made by that country or its administrative organs.<sup>217</sup> A decision allowing a member to block imports is, in effect, a judgment that the country's institutional arrangement is competent to make the decision on that kind of a question. A decision that prohibits a country from making a decision effectively allocates decision-making power elsewhere. And a decision that requires a member to consult with others before drawing a conclusion effectively establishes a different institutional arrangement for making such a choice. Under this vision, the Appellate Body is in the business of deciding who should determine various matters of policy.

A variant on this lens, one that also focuses on institutional

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*supra* note 3, at 5 (stating "on the one hand there are those who think that the approach has led to too rigid adherence to text, ignoring the intent of the negotiators. On the other hand, there are those who think that the Appellate Body has ignored the text and that its decisions are based on its own particular view of how trade should be liberalized").

<sup>216</sup> See Gregory Shaffer, *Power, Nested Governance, and the WTO: A Comparative Institutional Approach*, Mar. 1, 2004 (manuscript on file with the author); Shaffer & Apea, *supra* note 15, (analyzing the *EC-Preferences* case in terms of allocating institutional power to decide that nature of preference programs).

<sup>217</sup> *Id.*

competency to make the decision, recognizes that WTO members can reverse Appellate Body decisions. According to this view, Appellate Body decisions set up the negotiations among WTO members.<sup>218</sup> In a sense, the Appellate Body is deciding which member should have the burden of going forward in negotiations to secure a rule that would overturn the Appellate Body's interpretation. Because negotiations are the only method of reversing a decision of the Appellate Body, this effectively means that the Appellate Body is deciding which member or group within the WTO should have to pay to reverse the decision – that is, which country (or group of countries) should have to give up political and economic capital to have the result changed?

Under this vision, it is not surprising that the Appellate Body often seems to compromise in its decisions, allowing each side to claim a measure of victory and to absorb some measure of the cost of the decision.<sup>219</sup> One would expect this method of compromising in a system where it is clear that the result of the decision is to require the parties to negotiate over their rights and obligations, a process that is inherently fraught with compromise. Moreover, this proclivity to compromise is coupled with the recognition that the Appellate Body faces constraints that naturally lead it to be conservative and to minimize the use of its own power, including the need to promote the acceptability of its decisions to powerful countries.<sup>220</sup>

Our approach honors these institutional perspectives, but adds another dimension. As we demonstrate below, we believe that the Appellate Body recognizes that the WTO is a system in which members have unequal bargaining power and where bargaining is the basis of systemic equilibrium. Within this context, we see the Appellate Body functioning effectively as a kind of power broker in a system that would otherwise pit the powerful industrial countries against the less powerful developing countries. As we see it, within the confines of its interpretive space, the Appellate

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<sup>218</sup> See Richard H. Steinberg, *Judicial Lawmaking at the WTO: Discursive, Constitutional, and Political Constraints*, 98 AM. J. INT'L L. 247 (2004). See generally Carol J. Miller & Jennifer L. Croston, *WTO Scrutiny v. Environmental Objectives: Assessment of the International Dolphin Conservation Program Act*, 37 AM. BUS. L.J. 73 (1999) for examples of post-WTO decision negotiations.

<sup>219</sup> See Steinberg, *supra* note 218.

<sup>220</sup> See *id.*; Miller & Croston, *supra* note 218.

Body is crafting a jurisprudence of power and participation that allows it to adjust rights and responsibilities to reflect relative power, while recognizing the importance of both respecting and restraining power in the system. Under this view, the Appellate Body functions as an institutional gyroscope, one that provides balance in a system that, if unbalanced, could fall apart.

Our perspective is built on the understanding that the WTO regime must function as a rule-based regime (so that states will be willing to make commitments), but that binding commitments are made in anticipation of certain future benefits.<sup>221</sup> In this system, the continued success of the regime requires that gains for all members continue to outweigh losses, both *ex ante* (i.e. in advance of negotiations) and *ex post* (i.e. after the treaties are implemented). The reciprocity that is at the heart of the WTO system requires such balance.<sup>222</sup> Because bargaining power is inevitably influenced by economic strength, so too will the balance of gains and losses from the negotiations also be influenced. When the *ex post* world diverges from that expected *ex ante* world, the balance of gains and losses is likely to shift over time, and when it does, the allegiance to the future of the WTO regime also vacillates, with implications for both compliance with existing obligations and also the willingness to undertake new obligations. The role that the Appellate Body can effectively play in this regime is therefore to decide cases against a background that appreciates the political dynamics of the WTO, taking into account not only the legal arguments but also the position of the parties in terms of their role in the WTO regime. The Appellate Body's decisions not only distribute decision-making authority, but they also respond to, and influence, existing distributions of power.<sup>223</sup>

We therefore see the role of the Appellate Body to be that of a power broker—crafting a set of interpretive tools that seek to temper the power of industrial countries while not eliminating that

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<sup>221</sup> Gerhart, *supra* note 1167.

<sup>222</sup> See, e.g., Patrick Low, *Trading Free: The GATT and U.S. Trade Policy* 29 (1993) (discussing notions of fair trade and reciprocity, why they are sought through GATT tariff negotiations, and the difficulties the goal of reciprocity presents); The Future of the WTO, *supra* note 88, at 17 (“If [least developed countries] do not receive real benefit from membership there can be little point in their remaining part of the organization and the moral case for the WTO as a source of good is diminished.”)

<sup>223</sup> See *supra* notes 1 and 26 and accompanying text.

power as a force in shaping that international regime. The *EC-Conditional Preferences* decision demonstrates this thesis by showing that the Appellate Body has articulated its interpretive task to set up a jurisprudence of power and a jurisprudence of participation.<sup>224</sup>

#### A. *Jurisprudence of Power*

As we demonstrated above, GSP programs reflect the power relationship between developed and developing countries in two ways. First, GSP preferences are a gift, not an obligation, giving the donor countries the power to withdraw them at any time (a fact that in itself reflects the powerlessness of the poor countries).<sup>225</sup> Second, donor countries use the GSP preferences as an expression of their power by making the preferences contingent on conditions that benefit the donor country, but not the recipient country.<sup>226</sup> The Appellate Body has to respond to both expressions of power.

The Appellate Body's jurisprudence is a jurisprudence of power because the standard that will determine which conditions are acceptable is the standard that focuses on the well being of the recipient countries, taking into account their developmental, financial, and trade needs.<sup>227</sup> This creates a perfect match between the evaluative standard that will determine which conditions are permissible and the reasons the developing countries lack power. The developing countries lack power precisely because they have such great developmental, financial, and trade needs; addressing those needs addresses their lack of power.<sup>228</sup> This reading is not a radical or *ultra vires* interpretation of the Enabling Clause. Rather it is compelled by reading the Enabling Clause in the context of the negotiations that led to its enactment.<sup>229</sup>

Behind the legal issues is a difficult political issue that requires the Appellate Body to undertake a tenuous balancing act. Because the developed countries do not have to give preferences, any

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<sup>224</sup> European Communities—*Conditions for Granting Tariff Preferences to Developing Countries*, Report of the Appellate Body, WT/DS246/AB/R (April 7, 2004).

<sup>225</sup> See *supra* notes 73-74 and accompanying text.

<sup>226</sup> See *supra* notes 77-80 and accompanying text.

<sup>227</sup> See *supra* note 157 and accompanying text.

<sup>228</sup> See *supra* notes 149-154 and accompanying text.

<sup>229</sup> See *supra* notes 58-59.



attempt to restrict the conditions under which they offer the preferences could backfire and cause the developed countries to withdraw the preferences altogether. Moreover, because the GSP preferences have become a tool of political diplomacy—helping to shape the national policy of the recipient countries in ways that the donor country thinks are best—legislators who must approve the GSP programs are likely to resent any restrictions on their ability to influence what happens in the poorer countries. Having become acclimated to the notion of conditional preferences, they are unlikely to easily give up their ability to influence any policy of recipient countries that they find objectionable.

Moreover, the goals that donor countries seek to achieve with the conditions that they put on preferences are, in principle, often ones that are endorsed by the global community.<sup>230</sup> Arguably the EC could seek to justify its special incentive programs, promotion of labor rights and freedoms, environmental preservation, and the reduction of illicit drug production and trafficking contribute to the overall positive development of developing countries. One of the purposes behind the EC's GSP was to use this particular trade policy instrument as a means to address issues of sustainable development and to influence the social, environmental, and welfare aspects of trade.<sup>231</sup> A strong political interest therefore pulls in favor of allowing developed countries to have relative freedom in what conditions they impose when they give preferential treatment.

On the other hand, the intent of the Enabling Clause clearly was to restrict the donor country's use of conditions so that the preferences would be true gifts.<sup>232</sup> Conferring a benefit on

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<sup>230</sup> Numerous international institutions are working to achieve goals in the area of environmental labor rights, for example, giving the donor countries support for their argument that they are seeking no more than these international organizations seek. On the relationship between the WTO and these other areas of international law, see Symposium, *The Boundaries of the WTO*, 96 *Am. J. Int'l L.* 1 (2002).

<sup>231</sup> Further, in the words of the EC, trade is not an end in itself but a means to an end. For example, the EU linked trade to environmental standards in order to protect natural resources. *EU-LDC Themes – Social, Environmental & Welfare aspects of Trade Policy*, The EU-LDC Network, at [http://62.58.77.238/themes/socialwelfare/socialwelfare\\_policy.php](http://62.58.77.238/themes/socialwelfare/socialwelfare_policy.php) (last visited Oct. 29, 2003). The EC also reminded the WTO DSB that its special incentive arrangements were in line with internationally recognized objectives aimed at the promotion of sustainable development. *Id.*

<sup>232</sup> See generally Uche Ewelukwa, *Special and Differential Treatment in*

developing countries is the essence of the GSP system; to be effective, the preferences must confer benefits on the recipient countries and thus serve as a constant reminder of the benefits of membership in the WTO system that inure even to the powerless. If the conditions impose costs on the recipient country, they reduce the benefit of the preferences.<sup>233</sup> There must be some control on the use of preferences or the cost of the conditions could soon take away any benefit from the preferences.

Given these contradictory tendencies, the difficult role of the Appellate Body is to find a way to balance the legal requirement that the preferences be general, non-discriminatory and non-reciprocal, while at the same time recognizing the practical need to allow the donor countries to place some conditions on the receipt of the gifts.

### *B. Jurisprudence of Participation*

The Appellate Body's jurisprudence is also a jurisprudence of participation, for it emphasizes the right of developing countries – the powerless – to participate in shaping the programs that affect their future.<sup>234</sup>

One of the hallmarks of the Appellate Body's developing jurisprudence is the requirement that a country which proposes to take action implicating the interest of another member must first offer the other country basic procedures through which it can express its interests.<sup>235</sup> While this general requirement mirrors the many specific instances in which the covered treaties specifically mandate such procedures, the Appellate Body has frequently found a basis for inferring a requirement of due process when it is not otherwise specified in the treaties.<sup>236</sup> The *EC-Conditional*

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*International Trade Law: A concept in search of content*, 79 N.D. L. REV. 831 (2003) (discussing the Enabling Clause and special treatment for the least developed countries).

<sup>233</sup> See *supra* section II.B.

<sup>234</sup> See generally Jennifer L. Stamberger, *The Legality of Conditional Preferences to Developing Countries under the GATT Enabling Clause*, 4 CHI. J. INT'L L. 607 (2003) (addressing 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).

<sup>235</sup> Gerhart, *supra* note 1 at 61-70.

<sup>236</sup> *Id.*

*Preferences* case is only one example of a case in which this occurred; the requirement of some form of process where one country is making decisions that affect the interest of other countries has become a part of the unwritten constitution of the WTO.<sup>237</sup>

The right to participate is not just an abstraction. Participation is a source of power. Even those without substantial bargaining power can benefit if their right to participate is protected. Their reasoned argument may carry weight; their expressions of their own capacities, interests, and values may turn out to be persuasive. Even if their bargaining power is small, it will be greater when it can be expressed in a forum where others must listen. When the right to participate includes a number of countries, the bargaining power of one country can be magnified by being expressed in conjunction with the bargaining power of another country.

Not only are the procedural rights created by the Appellate Body a source of power for developing countries, the procedural requirements also allow the Appellate Body to influence the balance of power as they make judgments about whether the procedural requirements have been met in good faith.<sup>238</sup> Naturally, the procedural requirements do not themselves predetermine any particular outcome for the negotiations; the negotiations will still respond to the underlying power of the parties involved. But the procedural requirements do allow the Appellate Body to put its thumb on the scale of justice to determine whether the correct procedures have been followed in the correct way. The requirement that donor countries make explicit the basis on which the conditions they impose are thought to enhance the development, finance, and trade needs of recipient countries protects against decisions that are in the interest of donor but not recipient countries. The associated requirement that donor countries give potential recipient countries an opportunity to show that they meet the relevant criteria protects against arbitrary application of this criteria. The requirement that the list of beneficiary countries be held open<sup>239</sup> allows countries to avoid unjustifiable exclusion, and the requirement that beneficiary

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<sup>237</sup> *Id.*

<sup>238</sup> Howse, *Back to Court After Shrimp/Turtle*, *supra* note 12.

<sup>239</sup> *Id.*

countries be dropped from the list when the special preferences are no longer warranted<sup>240</sup> protects against uneven treatment of similarly situated countries. The Appellate Body controls the power relationship between strong and weak countries by controlling the terms under which strong countries make decisions that affect the weak countries.

## VII. Conclusion

The fundamental challenge facing the WTO regime is to construct a law-based system in the context of negotiations that are inevitably power-based. The regime must be law-based because the regime's success depends on inducing members to commit to change their domestic policy on the condition that other members will commit to change *their* policy. Member commitments are therefore constructed around expectations about the intentions and fidelity of other members. The mutual commitments at the heart of the WTO system are strengthened to the extent that international law can ensure that the expectations they embody will be fulfilled. When commitments are enforceable, members are induced to trust the commitments made by others and are therefore induced to increase their own commitments.

Negotiations of member commitments are inherently power-based, for the negotiations reflect the existing distribution of economic and, to some extent, political power.<sup>241</sup> Admittedly, the Uruguay Round agreements have made the WTO regime more "legalized" and the dispute settlement system has not only enhanced the legal certainty of the commitments made in the agreements, but (by making treaty interpretation power-neutral) has enhanced the power of the small countries. Yet even these strides have not removed economic and political power from the regime. Negotiations over new treaty commitments, whether to revise existing disciplines or to create new ones, continue to be based on economic power. The efforts of the WTO regime to limit the exercise of unilateral power within the law-based system have been only partially successful. The WTO regime, for example, has been unsuccessful at curbing the ability of the powerful countries to use bilateral and regional agreements to

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<sup>240</sup> *Id.*

<sup>241</sup> See *supra*, text accompanying notes 21 to 46

break up coalitions of developing countries and to influence multilateral negotiations. Even the new-found power and resolve of the developing countries, which is complicating the Doha Round of negotiations,<sup>242</sup> is a reflection of the importance of power on the system.

Moreover, even though existing obligations are subject to legalized dispute resolution that is independent of the power of the members, power continues to pervade the dispute settlement system as well. Power is inherent when countries make decisions about whether to challenge the conduct of another state, when they decide which states to sue, when they determine in pre-dispute resolution consultations how to achieve a “mutually agreed upon solution” and when they decide, after the legal process has won its course, whether to settle the case and how they will exercise their right to retaliate. Power is also implicated in the efficacy of retaliation; retaliation as a remedy does not favor the powerless states. Moreover, the dispute resolution system seems to be deeply affected by the cost and information requirements of bringing suit, which also disfavors the poorer states.

Because the WTO system involves lawmaking that reflects the economic power of the member countries, the poorer developing countries have long been at a disadvantage in the lawmaking process. They have not had much to offer to, nor have they been able to withdraw from, negotiations. As a result, they have had little opportunity to exert much influence over the course of the lawmaking. In the absence of some positive reason to participate in a system in which their participation was, in terms of influence, at best peripheral, the GATT system threatened to become one of wealthy countries and to forfeit the promise of becoming a force for global commerce.

The GSP system was carefully crafted to recognize the developing country's lack of relative power. As the Appellate Body astutely recognized, the system was designed to allow donor countries to give tariff concessions to poor countries without expecting to get anything in return. Such unilateral, donative preferences from states with power in the regime to states without power would address the lack of power of developing countries.

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<sup>242</sup> *Negotiations, implementation and development: the Doha agenda*, WTO at [http://www.wto.org/english/tratop\\_e/dda\\_e/dda\\_e.htm](http://www.wto.org/english/tratop_e/dda_e/dda_e.htm) (last visited Feb. 21, 2005).

These preferences would not only materially benefit the poor countries; the preferences would also strengthen the GATT/WTO regime. By giving tangible benefits to those with little power, the preferences would help ensure the allegiance of the developing states to the system and would thereby enhance the long-term stability for the system—a system whose long-run viability requires that each member have an opportunity to negotiate to increase its welfare.

The Appellate Body correctly interpreted the Enabling Clause to embody the fundamental principle that preferences are intended to be donative, not an exchange, and therefore to benefit the recipient countries only. Any benefit that the donor countries get must come from their understanding that their long-term interest is in the growth of the developing countries and in the breadth and stability that their allegiance to the WTO regime would instill.<sup>243</sup> This principle then guides the interpretation of the Enabling Clause when the Appellate Body is called on to determine whether conditions that donors placed on the preferences are for the benefit of the recipient country (and therefore lawful) or whether they are for the benefit of the donor country (and therefore impermissible). The legal standard recognized by the Appellate Body fully embodies the distributive thrust of the GSP program.

This standard inevitably requires the Appellate Body to make legal decisions in a political context. The fundamental legal issue—namely, whether the conditions under which the preferences are given truly address the development, financial and trade needs of the recipient country—is difficult enough. As we pointed out above, development experts have not agreed upon which policies really help developing countries, and the line between helpful and hurtful conditions is likely to be narrow. Although the guidelines that we suggested for making that determination can help bring clarity to the situation by, for example, putting an emphasis on conditions that are derived from development plans drawn up by countries in connection with international aid agencies, difficult legal judgments are inevitable.

Further complicating the legal judgments are the difficult underlying political issues. Donor countries will continue to condition preferences on policies in the developing countries that

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<sup>243</sup> See *supra* section II.B.

are in the donor country's interests. Because those conditions often reflect strongly held values in the donor country, the donor country's support for granting the preferences in the first place is likely to erode, and perhaps erode significantly, if the Appellate Body restricts too much those conditions. The Appellate Body thus walks a fine line. If it allows conditions on preferences that are too burdensome and one-sided, it risks allowing the system to turn from a donative system into a coercive system, where donor countries condition the preferences just up to the point where they become worthless. On the other hand, if it cuts back too severely on the conditions that are permissible, it runs that risk that donor countries will increasingly reduce the value of the preferences they give.

Fortunately, the Appellate Body has the tools to undertake this difficult legal and political balancing act.<sup>244</sup> By reserving to itself the ability to determine when the conditions on which preferences are given relate to the welfare of the developing countries, the Appellate Body, using its interpretive discretion, can effectively review conditional preferences to insure that they do not reflect the economic power of the donor countries. By requiring donor countries to be explicit and open in their decision-making,<sup>245</sup> the Appellate Body can insure that beneficiary countries have a genuine chance to benefit from the tariff preferences. At the same time, the Appellate Body can modulate its interpretations to make sure that tariff preferences continue to be offered by developed countries. In short, the Appellate Body is in a position to look out for the systemic interests of the WTO. This is entirely appropriate in the institutional context in which the Appellate Body operates. In retrospect, we can see that the real institutional innovation in the establishment of the Appellate Body was not just the creation of an independent judicial branch for the WTO. It was also the establishment of a quasi-judicial body that, in the process of interpretation, can understand the divergent interests of the individual members in a context that takes into account the needs for the WTO system to be balanced and mutually progressive.

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<sup>244</sup> See *supra* section VI.

<sup>245</sup> *Id.*

