Multilateral remedies for unilateral actions? Legal implications of United States' withdrawal of tariff preferences (GSP) for Indian exports: can India have any recourse at the WTO?

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Brief background

In April 2018, the Office of the United States Trade Representative (USTR) initiated a Country Practice Review regarding India's compliance with the United States' Generalized System of Preferences (GSP) eligibility criteria.[1] This review was based upon petitions from the National Milk Producers Federation, the U.S. Dairy Export Council and the Advanced Medical Technology Association, who alleged that India was not meeting the GSP eligibility criteria as mandated under US law. The primary task of the Country Practice Review was to focus on ascertaining whether or not India was meeting a specific GSP eligibility criterion – that of the GSP beneficiary providing an assurance of equitable and reasonable market access to United States' exports – the lack of which was expressly alleged in the stakeholder petitions.

Parallel to the submission of the petitions by the industry groups, the GSP Subcommittee of the Trade Policy Staff Committee (TPSC) had also self-initiated a review in order to evaluate India's compliance with the same GSP eligibility criterion. Both reviews were combined into one overall review of India's GSP eligibility, based on the market access requirement in the US GSP law. Public hearings were held during which the industry groups presented their views before the American authorities.

On 4 March 2019, the USTR announced that the US intended to terminate India's designation as a beneficiary developing country under the US GSP program as it no longer complied with the statutory eligibility criteria.[2] The USTR found that India had failed to "*provide the United States with assurances that it will provide equitable and reasonable access to its markets in numerous sectors.*"

The USTR notified the US Congress and the Government of India, and as per US law, the notification would be followed by a Presidential proclamation 60 days after the

announcement, which is when the withdrawal of the GSP benefits would take effect.[3] The 60-day period ended on 3 May 2019, but no proclamation was issued throughout May 2019. It is speculated that owing to the Parliamentary elections taking place in India, the US administration adopted a wait and watch attitude, although periodically reiterating its intention to withdraw India's status as a GSP beneficiary country. Finally, on 31 May 2019, the Trump administration issued a Presidential Proclamation withdrawing India's status as a beneficiary developing country under the US' GSP scheme.

This blog post will examine the potential legal issues that may arise subsequent to the US withdrawing tariff concessions for Indian exports, and discuss some arguments that India may advance in case it decides to seek recourse at the WTO.

What is the GSP and the Enabling Clause?

The GSP was first envisaged in a 1971 Decision[4] of the GATT Contracting Parties as a system based upon developed GATT parties extending "tariff preferences" (concessional tariff rates) to developing countries, in order to improve market access for developing countries' exports to the developed world. This was theorized as a method which would use trade as a tool to assist growth and development in such beneficiary developing countries, particularly led by the manufacturing of industrial goods.

Initially contemplated as a decade-long arrangement, the GSP was given a more comprehensive shape at the 1979 Tokyo Round negotiations, which led to the emergence of the Decision on Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries ("Enabling Clause").[5] The Enabling Clause was subsequently incorporated into the GATT 1994 as an "other decision" of the GATT 1947 Contracting Parties.[6] In the *EC – Tariff Preferences* case, the WTO Appellate Body (AB) recognised that the Enabling Clause had become an "integral part" of the GATT 1994.[7] Overall, the Enabling Clause broadly remains the overarching legal framework under the GATT/WTO regime governing any GSP schemes that WTO members may operate.

What could India challenge at the WTO in the present case?

If India were to challenge the withdrawal of benefits accorded to its exports under the American GSP scheme, the measures at issue could include both the Presidential

Proclamation, as well as the statutory provision invoked to justify the withdrawal of India as a GSP beneficiary country (Section 502 (c)(4) of the Trade Act, 1974). These are the instruments of US law constituting the background to the actions culminating in the withdrawal of GSP benefits for Indian exports, and would thus constitute the measures at issue.

Will the withdrawal of GSP benefits for Indian exports be in conformity with the 'non-reciprocity' requirements in footnote 3, paragraph 2(a) and paragraph 5 of the Enabling Clause?

No WTO member has an obligation to administer a GSP program and grant preferential tariffs to developing/least-developed countries. However, in case a WTO member desires or decides to administer a GSP program, the contours of such a program must conform to the requirements of the legal framework governing such GSP programs – i.e. the requirements of the Enabling Clause.

Footnote 3 to paragraph 2(a) essentially provides that only preferential tariff treatment that is "generalized, non-reciprocal and non-discriminatory" is covered under paragraph 2(a) of the Enabling Clause. Further, paragraph 5 of the Enabling Clause comprehensively reinforces the basic understanding of tariff preferences for developing countries by the developed countries as being founded on "non-reciprocity":

5. *The developed countries do not expect reciprocity for commitments made by them in trade negotiations to reduce or remove tariffs and other barriers to the trade of developing countries, i.e., 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. Developed contracting parties shall therefore not seek, neither shall less-developed contracting parties be required to make, concessions that are inconsistent with the latter's development, financial and trade.*

As far as the "generalized, non-reciprocal and non-discriminatory" terminology is concerned, the WTO Appellate Body (AB) in *EC - Tariff Preferences* did interpret the requirement of a tariff preference scheme to be "non-discriminatory", but expressly refrained from commenting upon *"whether the Enabling Clause permits ab initio exclusions from GSP schemes of countries claiming developing country status, or the partial or total withdrawal of GSP benefits from certain developing countries under certain conditions."*[8]

To date, there is no authoritative legal interpretation of the "non-reciprocal" requirement under the Enabling Clause. In this post, I adopt the interpretation of "non-discriminatory" as developed by the AB, offer an additional dimension to that interpretation, and finally argue that such an interpretation of "non-discriminatory" can be further extended to serve as a guiding light to interpret the "non-reciprocal" requirement under the Enabling Clause.

In *EC – Tariff Preferences,* the AB noted that action distinguishing among similarly-situated GSP beneficiaries is discriminatory in nature.[9] However, the AB also found that the "non-discriminatory" requirement should not be interpreted in a manner which requires GSP donors to grant identical tariff preferences to all GSP beneficiaries.[10] In this regard, the AB highlighted that the Enabling Clause does impose certain specific *conditions* on the grant of differential tariff preferences among GSP beneficiaries.

Therefore, one important dimension that can be culled out of the AB's interpretation of "non-discriminatory" is that "*unconditional"* is not a necessary pre-requisite for a preference scheme to be "non-discriminatory" under the Enabling Clause. In other words, imposing conditions does not, by and of itself, make a scheme discriminatory. It is the content and requirements laid down by the conditions that may be found to bediscriminatory. Arguably, such an understanding may be extended in order to assist in the interpretation of the non-reciprocity requirement under the Enabling Clause as well.

Consequently, "non-reciprocal" should not be understood to entirely prohibit GSP donor countries from attaching any conditions to the grant of preferences to GSP beneficiaries. A developed country imposing conditions that a beneficiary country has to comply with in order to be eligible for GSP preferences does not *per se* violate the "non-reciprocal" requirement. However, "non-reciprocity" is violated if the imposed conditions are *themselves* founded on reciprocity – i.e. if they are, for all purposes, a *quid pro quo* arrangement. Secondly, the conditions also need to be contextualized with the express stipulations of the Enabling Clause – they should not be "inconsistent with the development, financial and trade needs" of the particular developing country.

Thus, a combined reading of the "non-reciprocity" requirement as enshrined in paragraph 2(a) and paragraph 5, as developed by the above analysis, leads to the following understanding:

1. A developed country imposing conditions that a beneficiary country has to comply with in order to be eligible for GSP preferences does not *per se* violate the "non-reciprocal" requirement under paragraph 2(a) and paragraph 5 of the Enabling Clause.
2. Any imposition of conditions, or modification of conditions of eligibility, for GSP beneficiary status should be consistent with the development, financial and trade needs of the developing country.
3. Conditions which are themselves founded on reciprocity, i.e. *quid pro quo* arrangements, will run afoul of the "non-reciprocal" requirement.

In light of this discussion, can the US invoke claims of alleged market-access barriers for other products (unrelated to the GSP scheme) in India, as a ground to legally revoke tariff preferences to Indian exports under the US' GSP program? Arguably, no.

First, it is submitted that the US may well be justified in imposing certain conditions mandating that a potential beneficiary country provide it "equitable and reasonable access" to its market (as the wording of Section 502 (c)(4) of the Trade Act of 1974 provides).[11] Thus, mandating "equitable and reasonable access" by *itself* does *not* amount to a violation of the overarching principle of "non-reciprocity" that governs the donor-beneficiary relationship under the GSP schemes.

However, the threshold for meeting any such requirement of "equitable and reasonable access" by any developing country must arguably be set low (in order to conform to the overarching principle of non-reciprocity). Thus, as long as the reciprocal market access sought is limited to general, "equitable and reasonable" market access conditions (which may be interpreted to mean the absence of overtly protectionist market entry barriers, etc.), it is not a *quid pro quo* demand and does not violate non-reciprocity.

However, in this specific case, demanding market access for the dairy sector and the pharmaceutical and medical devices industries, and making GSP benefits for the entire range of Indian exports specifically *contingent* on such market access, would run afoul of the overarching non-reciprocity requirement. The demand for greater sector-specific market access liberalisation is in itself a *quid pro quo* demand and thus violative of the principle of "non-reciprocity" as enshrined in the Enabling Clause. Further, seeking such *quid pro quo* concessions also violates the obligation of a GSP donor to not seek "concessions that are inconsistent with the development, financial and trade needs" of the beneficiary developing country. This argument shall be further elaborated in the next section of this post.

Will the withdrawal of GSP benefits be in conformity with paragraph 3(c) of the Enabling Clause? Specifically, is the withdrawal of the GSP benefits a "modification" that "responds positively" to the "development, financial and trade needs" of developing countries?

Paragraph 3(c) of the Enabling Clause provides:

3. *Any differential and more favourable treatment provided under this clause: c) shall in the case of such treatment accorded by developed contracting parties to developing countries be designed and, if necessary, modified, to respond positively to the development, financial and trade needs of developing*

'Conditionalities' in GSP schemes and their legality

The GSP programs administered by the USA and the EU are two of the most prominent GSP schemes globally. Both the EU and the US regulate the grant of trade preferences under their GSP schemes by imposing certain conditions on the beneficiary developing countries. These are known as 'conditionalities' associated with the GSP scheme.

The US attaches conditions for developing countries to be eligible for preferential tariffs under the American GSP program. Unlike the so-called "positive conditionalities" (which were the measures at issue in the *EC – Tariff Preferences* case) - which is a regime which provides *additional* preferences to eligible countries which fulfil certain extra requirements, the US regulations largely provide for "negative conditionalities", i.e. conditions which, if not met, would make a developing country *ineligible* for being considered for designation as a GSP beneficiary under the GSP program in the first place. While the EU GSP program also provides for certain negative conditionalities, they are more prominent in the American GSP program.

These negative conditionalities which make a country ineligible to receive preferential tariffs under the US GSP program broadly include the existence of a communist regime in the country (with exceptions), giving preferential tariffs to developed country products, expropriation of American Intellectual Property Rights (IPRs), repudiation of American contracts, non-enforcement of arbitral awards, lax implementation of child labour elimination norms, and providing sanctuary to international terrorists.[12] Further, the US statute which governs the GSP program also lays down certain factors "affecting" country designation, including an assessment of the *"extent to which such country has assured the United States that it will*

provide equitable and reasonable access to the markets." (Section 502 (c)(4) of the Trade Act, 1974, as amended).

It is important to draw a distinction in the US statutory provisions between the conditionalities which would regulate a finding of "*Countries ineligible for designation*", versus certain other "*Factors affecting country designation*". Using astute drafting, the American statute tries to maintain a fine line of difference between the *conditions* it has set for a developing country to be eligible for GSP benefits, and "*other factors*" (which offer a greater level of discretion to the President) which would assist the President in arriving at a conclusion about a developing country's eligibility to avail GSP benefits.

However, for the purposes of determining compliance with the substantive rules of the Enabling Clause, *both* the conditions as well as the other factors laid down in the US statute must be found to comply with the Enabling Clause. Therefore, for the present purposes, all these criteria – conditions, as well as other factors, shall be considered as 'conditionalities' that a developing country must fulfil in order to be eligible for GSP benefits.

It is important to recognize that the Enabling Clause does not envisage absolutely *unconditional* tariff preferences being offered to developing countries by developed countries. As mentioned earlier, one way to understand the AB's interpretation in *EC – Tariff Preferences* is that "unconditional" is not a necessary prerequisite for a preference scheme to be "non-discriminatory". Establishing conditions that a developing country must meet in order to be eligible for GSP benefits does not, by and of itself, make a scheme discriminatory (or violate the Enabling Clause in any manner). It is instead the content and requirements laid down by the conditions that may be found to be discriminatory.

Therefore, conditionalities attached to GSP schemes are legal. However, the test under paragraph 3(c) of the Enabling Clause that any such conditionality has to fulfil is that it must "*respond positively to the development, financial and trade needs*" of the developing countries. The test laid down by the Appellate Body in *EC – Tariff Preferences* to evaluate the compatibility of differential treatment in donor countries' GSP schemes was twofold - such differential treatment/conditionalities must respond positively to the development, financial, and trade needs of developing country GSP beneficiaries, and, secondly, it must be applied equally to similarly situated beneficiaries, seen in terms of their development, financial, and trade needs. Again,

the AB's understanding of the scope of differential treatment among GSP beneficiaries can be further developed and applied to our understanding of"conditionalities".

Proving that a conditionality responds "*positively to the development, financial and trade needs*" of developing countries is an onerous obligation, and arguably, the burden of proof in such a case would lie on the GSP donor – thus, if challenged, it is the US which will have to show that the impugned conditionality is consistent with the obligation of responding "*positively to the development, financial and trade needs*" of India.

Does the US negative conditionality (requiring equitable and reasonable market access) respond "positively" to the "development, financial and trade needs of India"? Arguably, no.

Positive conditionality schemes (for example, those which grant greater tariff reductions over and above the general preferential tariffs, if the beneficiary developing countries take extra efforts to protect the environment, enforce higher labour standards etc.) clearly respond "positively" to the "development, financial and trade needs" of the beneficiary developing countries. Even negative conditionality schemes may be designed in such a manner that they respond "positively" to the "development, financial and trade needs" of a developing country (for example, a GSP scheme which envisages revocation of a country's designation as a GSP beneficiary if such country is found to allow and encourage child labour).

However, the provision of the GSP scheme at hand and its specific application in this case cannot be said to fulfil the requirements of paragraph 3(c) of the Enabling Clause. While other negative conditionalities in the same US GSP scheme (such as those relating to non-enforcement of arbitral awards, lax implementation of child labour elimination norms, and sanctuary to international terrorists) are such negative conditionalities which would arguably *fulfil* the requirement of responding "positively" to the "development, financial and trade needs" of beneficiary developing countries, the conditionality relating to guarantees of reciprocal market access – for all purposes, a *quid pro quo* – clearly does not.

Additionally, it would be helpful to locate a specific set of circumstances which can fall within the ambit of a "development, financial and trade need" of India, that would be unquestionably adversely affected by the withdrawal of GSP benefits. In this regard,

it may be relevant that the Indian industries manufacturing the products that ultimately avail the preferential tariffs under the US' GSP scheme are generally small and medium enterprises (SMEs). Such SMEs form the backbone of the Indian economy and provide gainful employment and a source of livelihood to hundreds of thousands of people. Consequently, any withdrawal of preferential treatment to exports being manufactured by such SMEs is bound to have a negative impact on the continuing viability of such SMEs.

Thus, a negative conditionality which makes reciprocal market access a prerequisite for grant of benefits, and then goes on to specify the particular sectors in which India must give the GSP donor greater market access in order to *continue* to be eligible to receive GSP benefits, cannot be said to respond "positively" to the "development, financial and trade needs" of India. Secondly, the direct, adverse impacts of such an action (withdrawal of benefits) to the overall economic structure of the GSP beneficiary (India) also illustrate that such an action does not to respond "positively" to the "development, financial and trade needs" of the GSP beneficiary.

Conclusion

As per reasonable legal interpretations of the Enabling Clause and guidance of the AB's decision in *EC – Tariff Preferences*, India may have a remedy at the WTO, and a WTO Panel may find the US withdrawal of India's designation as a GSP beneficiary to be violative of certain provisions of the Enabling Clause. Specifically, the withdrawal of GSP benefits may not be in conformity with paragraph 2(a), paragraph 3(c) and paragraph 5 of the EnablingClause.

However, this issue cannot be seen only from the perspective of legal regulation. The United States' decision to withdraw India's designation as a beneficiary country from its GSP program arguably stems more from peripheral reasons, and the overall trade relationship between the two countries, rather than simply India's compliance with the legal requirements under US statutory law. Crudely put, the US is using the threat of GSP withdrawal as a leverage to negotiate increased market access in India, which had seen a setback after India took unprecedented steps in imposing price controls on the medical devices industry. The perennially thorny issues of IPRs, data localization, agricultural market access etc. between the two countries also loom large in the background to such a decision.

It is also interesting to note that the stakeholders pressing for such revocation were American *exporters* lobbying[13] the US government for increased market access into India, and not American *importers* who could be threatened by competition (cheap Indian imports under the GSP program). On the other hand, American industries have been lobbying the US government for GSP benefits to India to continue, as it helps them utilize the cheaper imports of intermediary products (under the GSP program, and particularly from India) in producing final goods and export them at competitive rates in the world market.[14]

Ultimately, while India may seek WTO dispute settlement in case of withdrawal of its GSP designation, the approach, outcome and consequences of such a dispute will be uncertain at best. In this specific case, a more enduring solution might be found by continued trade negotiations at the political level between the two countries on GSP (and on the whole range of trade issues), rather than by legal wrangling.

[1] Federal Register/Vol. 83, No. 82/Friday, April 27, 2018/Notices - Office of the United States Trade Representative [Docket Numbers USTR–2018–0006, 2018–007, and 2018–008] Initiation of Country Practice Reviews of India, Indonesia, and Kazakhstan <https://www.govinfo.gov/content/pkg/FR-2018-04-27/pdf/2018-08868.pdf> accessed 13 June 2019.

[2] Office of the USTR, 'United States Will Terminate GSP Designation of India and Turkey', 4 March 2019, <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2019/march/united-states-will-terminate-gsp> accessed 13 June 2019.

[3] Section 502 (f)(2) of the Trade Act of 1974.

[4] Decision of the Contracting Parties of 25 June 1971, BISD 18S/24.

[5] Differential And More Favourable Treatment Reciprocity And Fuller Participation Of Developing Countries, Decision of 28 November 1979, L/4903 [Enabling Clause].

[6] Para. 1(b)(iv) of Annex 1A to the WTO Agreement incorporating the GATT 1994 into the WTO Agreement.

[7] *European Communities – Conditions For The Granting Of Tariff Preferences To Developing Countries* – Report of the Appellate Body (7 April 2004) WT/DS246/AB/R [90].

[8] *European Communities – Conditions For The Granting Of Tariff Preferences To Developing Countries* –Report of the Appellate Body (7 April 2004) WT/DS246/AB/R [129].

[9] *European Communities – Conditions For The Granting Of Tariff Preferences To Developing Countries* –Report of the Appellate Body (7 April 2004) WT/DS246/AB/R [153].

[10] *European Communities – Conditions For The Granting Of Tariff Preferences To Developing Countries* –Report of the Appellate Body (7 April 2004) WT/DS246/AB/R [156].

[11] Section 502 (c)(4) of the Trade Act of 1974.

[12] Section 502(b)(2)(A)-(H), Trade Act of 1974.

[13] Such as AdvaMed, National Milk Producers Federation, U.S. Dairy Export Council, Alliance for Fair Trade with India. See the verbatim record of the Public Country Practice Hearing for the U.S. GSP, June 19, 2018.

[14] As evident from the submissions of U.S. lobby groups such as the GSP Action Committee, U.S.-India Strategic Partnership Forum, American Apparel & Footwear Association etc. See the verbatim record of the Public Country Practice Hearing for the U.S. GSP, June 19, 2018.