

# **International and Regional Trade Law: The Law of the World Trade Organization**



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## **Unit IV: Tariffs and Customs Law / The Most-Favored Nation Principle**

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### **Table of Contents**

1.	Tariffs and Customs Law.....	4
1-1.	Introduction.....	4
	Relevant Provisions .....	4
	Overview.....	5
	Harmonized System (HS) .....	7
	Technical Information on Customs Valuation.....	8
1-2.	European Communities -- Customs Classification of Certain Computer Equipment (LAN Case) .....	9
	Summary of Facts .....	9
	Appellate Body Report .....	10
2.	The Most Favored Nation Principle.....	25
2-1.	Introduction.....	25
	Relevant Provisions .....	25
	Origin of the Most-Favored Nation (MFN) Principle.....	26
2-2.	Spanish Coffee .....	27
2-3.	Japan – Lumber.....	35
2-4.	Exceptions.....	38
	Regionalism (cf. Unit 2) .....	38
	Enabling Clause for developing countries (goods).....	38
	Waivers .....	40
	European Communities -- Conditions for the Granting of Tariff Preferences to Developing Countries (EC -- Tariff Preferences).....	42
3.	Optional Reading .....	67

### **Supplementary Reading**

For a more complete overview over the WTO law on tariffs and customs and the most-favored nation principle we suggest the following reading:

*Peter van den Bossche, The Law and Policy of the World Trade Organization, 2005, 309-318; 377-441.*

*Raj Bhala, Modern GATT Law. A Treatise on the General Agreement on Tariffs and Trade, 2005, 173-337.*

*Michael J. Trebilcock & Robert Howse, The Regulation of International Trade, 3rd ed. 2005, 177-193; 49-82.*

*John H. Jackson et al., Legal Problems of International Economic Relation, 4th ed. 2002, Chapter 8, 338-386; Chapter 10, 415-446.*

*John H. Jackson, The World Trading System, 2nd ed. 1997, 139-153; 157-173.*

# **1. Tariffs and Customs Law**

## 1-1. INTRODUCTION

### **Relevant Provisions**

Read in the Primary Sources:

- Article II GATT 1994
- Interpretative note *Ad* Article II (GATT Annex I)
- Article VII GATT 1994
- Interpretative note *Ad* Article VII (GATT Annex I)
- Introduction and Articles 1-8, 18-19 of the Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade 1994
- Understanding on the Interpretation of Article II:1(b) of the General Agreement on Tariffs and Trade 1994

## Overview

From the WTO publication “Understanding the WTO” (last revised February 2007)

[http://www.wto.org/english/thewto\\_e/whatis\\_e/tif\\_e/agrm2\\_e.htm](http://www.wto.org/english/thewto_e/whatis_e/tif_e/agrm2_e.htm)

### Tariffs - more bindings and closer to zero

The bulkiest results of Uruguay Round are the 22,500 pages listing individual countries' commitments on specific categories of goods and services. These include commitments to cut and “bind” their customs duty rates on imports of goods. In some cases, tariffs are being cut to zero. There is also a significant increase in the number of “bound” tariffs — duty rates that are committed in the WTO and are difficult to raise.

#### Tariff cuts

Developed countries' tariff cuts were for the most part phased in over five years from 1 January 1995. The result is a 40% cut in their tariffs on industrial products, from an average of 6.3% to 3.8%. The value of imported industrial products that receive duty-free treatment in developed countries will jump from 20% to 44%.

There will also be fewer products charged high duty rates. The proportion of imports into developed countries from all sources facing tariffs rates of more than 15% will decline from 7% to 5%. The proportion of developing country exports facing tariffs above 15% in industrial countries will fall from 9% to 5%.

The Uruguay Round package has been improved. On 26 March 1997, 40 countries accounting for more than 92% of world trade in [information technology products](#), agreed to eliminate import duties and other charges on these products by 2000 (by 2005 in a handful of cases). As with other tariff commitments, each participating country is applying its commitments equally to exports from all WTO members (i.e. on a [most-favoured-nation](#) basis), even from members that did not make commitments.

#### More bindings

Developed countries increased the number of imports whose tariff rates are “[bound](#)” (committed and difficult to increase) from 78% of product lines to 99%. For developing countries, the increase was considerable: from 21% to 73%. Economies in transition from central planning increased their bindings from 73% to 98%. This all means a substantially higher degree of market security for traders and investors.

> [more on market access](#)

> See also [Doha Agenda negotiations](#)

#### And agriculture ...

Tariffs on all agricultural products are now bound. Almost all import restrictions that did not take the form of tariffs, such as quotas, have been converted to tariffs — a process known as “tariffication”. This has made markets substantially more predictable for agriculture. Previously more than 30% of agricultural produce had faced quotas or import restrictions. The first step in “tariffication” was to replace these restrictions with tariffs that represented about the same level of protection. Then, over six years from 1995-2000, these tariffs were gradually reduced (the reduction period for developing countries ends in 2005). The market access commitments on agriculture also eliminate previous import bans on certain products.

In addition, the lists include countries’ commitments to reduce domestic support and export subsidies for agricultural products. (*See section on [agriculture](#).*)

## Harmonized System (HS)

*From the World Customs Organization (WCO) Website*

[http://www.wcoomd.org/ie/en/topics\\_issues/harmonizedsystem/hsconve2.html](http://www.wcoomd.org/ie/en/topics_issues/harmonizedsystem/hsconve2.html)

The Harmonized Commodity Description and Coding System, generally referred to as "Harmonized System" or simply "HS", is a multipurpose international product nomenclature developed by the World Customs Organization (WCO). It comprises about 5,000 commodity groups, each identified by a six digit code, arranged in a legal and logical structure and is supported by well-defined rules to achieve uniform classification. The system is used by more than 190 countries and economies as a basis for their Customs tariffs and for the collection of international trade statistics. Over 98 % of the merchandise in international trade is classified in terms of the HS.

The HS contributes to the harmonization of Customs and trade procedures, and the non-documentary trade data interchange in connection with such procedures, thus reducing the costs related to international trade. It is also extensively used by governments, international organizations and the private sector for many other purposes such as internal taxes, trade policies, monitoring of controlled goods, rules of origin, freight tariffs, transport statistics, price monitoring, quota controls, compilation of national accounts, and economic research and analysis. The HS is thus a universal economic language and code for goods, and an indispensable tool for international trade.

The Harmonized System is governed by "The International Convention on the Harmonized Commodity Description and Coding System". The official interpretation of the HS is given in the Explanatory Notes (4 volumes in English and French) published by the WCO. The Explanatory Notes are also available on CD-ROM, as part of a commodity database giving the HS classification of more than 200,000 commodities actually traded internationally.

The maintenance of the HS is a WCO priority. This activity includes measures to secure uniform interpretation of the HS and its periodic updating in light of developments in technology and changes in trade patterns. The WCO manages this process through the Harmonized System Committee (representing the Contracting Parties to the HS Convention), which examines policy matters, takes decisions on classification questions, settles disputes and prepares amendments to the Explanatory Notes. The HS Committee also prepares amendments updating the HS every 4 – 6 years.

Decisions concerning the interpretation and application of the Harmonized System, such as classification decisions and amendments to the Explanatory Notes or to the Compendium of Classification Opinions, become effective two months after the approval by the HS Committee. These are reflected in the amending supplements of the relevant WCO publications and can also be found on this web site.

## **Technical Information on Customs Valuation**

*From the WTO Website*

[http://www.wto.org/english/tratop\\_e/cusval\\_e/cusval\\_info\\_e.htm](http://www.wto.org/english/tratop_e/cusval_e/cusval_info_e.htm)

### **Specific and ad valorem customs duties**

Customs duties can be designated in either specific or ad valorem terms or as a mix of the two. In case of a specific duty, a concrete sum is charged for a quantitative description of the good, for example USD 1 per item or per unit. The customs value of the good does not need to be determined, as the duty is not based on the value of the good but on other criteria. In this case, no rules on customs valuation are needed and the Valuation Agreement does not apply. In contrast, an ad valorem duty depends on the value of a good. Under this system, the customs valuation is multiplied by an ad valorem rate of duty (e.g. 5 per cent) in order to arrive at the amount of duty payable on an imported item.

### **Definition**

Customs valuation is a customs procedure applied to determine the customs value of imported goods. If the rate of duty is ad valorem, the customs value is essential to determine the duty to be paid on an imported good.

### **Short historical overview**

#### **Article VII GATT**

Article VII of the General Agreement on Tariffs and Trade laid down the general principles for an international system of valuation. It stipulated that the value for customs purposes of imported merchandise should be based on the actual value of the imported merchandise on which duty is assessed, or of like merchandise, and should not be based on the value of merchandise of national origin or on arbitrary or fictitious values. Although Article VII also contains a definition of “actual value”, it still permitted the use of widely differing methods of valuing goods. In addition, ‘grandfather clauses’ permitted continuation of old standards which did not even meet the very general new standard.

(...)

## 1-2. EUROPEAN COMMUNITIES -- CUSTOMS CLASSIFICATION OF CERTAIN COMPUTER EQUIPMENT (LAN CASE)

*This dispute deals with the correct interpretation of a negotiated tariff concession.*

*The US relied very strongly on the legitimate expectations argument. But did they really mean legitimate expectations? Which arguments should the US have made -- consistent with the rules on interpretation -- to support their claim that LAN equipment falls under automatic data processing machines and not telecommunications equipment?*

*Assuming that the AB was correct in holding that one cannot rely on legitimate expectations, but has to look at what the parties have agreed on, what should be the result of the case?*

### **Summary of Facts**

*from a Case Note by Joel P. Trachtman, (<http://www.ejil.org/journal/Vol9/No2/sr5.html>)*

This decision concerns the tariff treatment of local area network (“LAN”) equipment and personal computers with multimedia capability (“PCs with multimedia capability”). At the core of this dispute was the question of whether LAN equipment fell under heading 84.71 of the European Communities (“EC”) tariff schedule, relating to automatic data processing machines and units thereof (“ADP machines”), or whether, as the EC argued, this equipment was properly included under heading 85.17, relating to telecommunications equipment. Customs duties are generally higher on the latter. Indeed, this case explores the intersection between computation and communication.

(...)

The U.S. complaint argued that from June 1995, pursuant to an EC Commission regulation, certain EC customs authorities (notably the British and Irish) changed their tariff treatment of imports of LAN equipment, previously dutiable under heading 84.71 as ADP machines, to rates applicable to heading 85.17, referring to telecommunications equipment. In addition, the U.S. argued that customs authorities had increased tariffs on certain PCs with multimedia capability from heading 84.71 to other categories bearing higher duties.

## Appellate Body Report

WT/DS62,67,68/AB/R, 5 June 1998

*Editorial Note: The footnote numbering does not correspond to the footnote numbering in the original report.*

Appellate Body Division: Beeby, Ehlermann and Lacarte-Muró

[http://www.wto.org/english/tratop\\_e/dispu\\_e/cases\\_e/ds62\\_e.htm](http://www.wto.org/english/tratop_e/dispu_e/cases_e/ds62_e.htm)

### I. Introduction

1. The European Communities appeals from certain issues of law covered in the Panel Report, *European Communities - Customs Classification of Certain Computer Equipment*<sup>173</sup> (the "Panel Report") and certain legal interpretations developed by the Panel in that Report. The Panel was established to consider complaints by the United States against the European Communities, Ireland and the United Kingdom concerning the tariff treatment of Local Area Network ("LAN") equipment and personal computers with multimedia capability ("PCs with multimedia capability").<sup>174</sup> The United States claimed that the European Communities, Ireland and the United Kingdom accorded to LAN equipment and/or PCs with multimedia capability treatment less favourable than that provided for in Schedule LXXX of the European Communities<sup>175</sup> ("Schedule LXXX") and, therefore, acted inconsistently with their obligations under Article II:1 of the *General Agreement on Tariffs and Trade 1994* (the "GATT 1994").

2. The Panel Report was circulated to the Members of the World Trade Organization (the "WTO") on 5 February 1998. The Panel reached the conclusion that:

... the European Communities, by failing to accord imports of LAN equipment from the United States treatment no less favourable than that provided for under heading 84.71 or heading 84.73, as the case may be, in Part I of Schedule LXXX, acted

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<sup>173</sup>WT/DS62/R, WT/DS67/R and WT/DS68/R, 5 February 1998.

<sup>174</sup>The United States submitted three requests for the establishment of a panel: *European Communities - Customs Classification of Certain Computer Equipment*, WT/DS62/4, 13 February 1997; *United Kingdom - Customs Classification of Certain Computer Equipment*, WT/DS67/3, 10 March 1997; and *Ireland - Customs Classification of Certain Computer Equipment*, WT/DS68/2, 10 March 1997. At its meeting of 20 March 1997, the Dispute Settlement Body (the "DSB") agreed to modify, at the request of the parties to the dispute, the terms of reference of the Panel established against the European Communities, so that the panel requests by the United States contained in documents WT/DS67/3 and WT/DS68/2 might be incorporated into the mandate of the Panel established pursuant to document WT/DS62/4. See WT/DS62/5, 25 April 1997.

<sup>175</sup>Schedule LXXX of the European Communities, *Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations*, done at Marrakesh, 15 April 1994.

inconsistently with the requirements of Article II:1 of GATT 1994.<sup>176</sup>

The Panel made the following recommendation:

The Panel recommends that the Dispute Settlement Body request the European Communities to bring its tariff treatment of LAN equipment into conformity with its obligations under GATT 1994.<sup>177</sup>

3. On 24 March 1998, the European Communities notified the DSB<sup>178</sup> of its intention to appeal certain issues of law covered in the Panel Report and legal interpretations developed by the Panel, pursuant to paragraph 4 of Article 16 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU"), and filed a Notice of Appeal with the Appellate Body, pursuant to Rule 20 of the *Working Procedures for Appellate Review* (the "*Working Procedures*"). On 3 April 1998, the European Communities filed an appellant's submission.<sup>179</sup> On 20 April 1998, the United States filed an appellee's submission<sup>180</sup> and on the same day, Japan filed a third participant's submission.<sup>181</sup> The oral hearing, provided for in Rule 27 of the *Working Procedures*, was held on 27 April 1998. At the oral hearing, the participants and the third participant presented their arguments and answered questions from the Division of the Appellate Body hearing the appeal.

(...)

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<sup>176</sup>Panel Report, para. 9.1.

<sup>177</sup>Panel Report, para. 9.2.

<sup>178</sup>WT/DS62/8, WT/DS67/6 and WT/DS68/5, 24 March 1998.

<sup>179</sup>Pursuant to Rule 21(1) of the *Working Procedures*.

<sup>180</sup>Pursuant to Rule 22 of the *Working Procedures*.

<sup>181</sup>Pursuant to Rule 24 of the *Working Procedures*.

### **III. Issues Raised in this Appeal**

57. The appellant, the European Communities, raises the following issues in this appeal:

(...)

- (b) Whether the Panel erred in interpreting Schedule LXXX, in particular, by reading Schedule LXXX in the light of the "legitimate expectations" of an exporting Member, and by considering that Article II:5 of the GATT 1994 confirms the interpretative value of "legitimate expectations"; and
- (c) Whether the Panel erred in putting the onus of clarifying the scope of a tariff concession during a multilateral tariff negotiation conducted under the auspices of the GATT/WTO, solely on the importing Member.

(...)

### **V. "Legitimate Expectations" in the Interpretation of a Schedule**

74. The European Communities also submits that the Panel erred in interpreting Schedule LXXX, in particular, by:

- (a) reading Schedule LXXX in the light of the "legitimate expectations" of an exporting Member; and
- (b) considering that Article II:5 of the GATT 1994 confirms the interpretative value of "legitimate expectations".

Subordinately, the European Communities submits that the Panel erred in considering that the "legitimate expectations" of an exporting Member with regard to the interpretation of tariff concessions should be based on the classification practices for individual importers and individual consignments, or on the subjective perception of a number of exporting companies of that exporting Member.

75. Schedule LXXX provides tariff concessions for ADP machines under headings 84.71 and 84.73 and for telecommunications equipment under heading 85.17. The customs duties set forth in Schedule LXXX on telecommunications equipment are generally higher than those on ADP machines.<sup>182</sup> We note that Schedule LXXX does not contain any explicit reference to "LAN equipment" and that the European Communities currently treats LAN equipment as telecommunications equipment. The United States, however, considers that the EC tariff concessions on ADP machines, and not its tariff concessions on telecommunications equipment, apply to LAN equipment. The United States claimed before the Panel, therefore, that the European Communities accords to imports of LAN equipment treatment less favourable than that

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<sup>182</sup>See Panel Report, paras. 2.10 and 8.1.

provided for in its Schedule, and thus has acted inconsistently with Article II:1 of the GATT 1994. The United States argued that the treatment provided for by a concession is the treatment reasonably expected by the trading partners of the Member which made the concession.<sup>183</sup> On the basis of the negotiating history of the Uruguay Round tariff negotiations and the actual tariff treatment accorded to LAN equipment by customs authorities in the European Communities during these negotiations, the United States argued that it reasonably expected the European Communities to treat LAN equipment as ADP machines, not as telecommunications equipment.

76. The Panel found that:

... for the purposes of Article II:1, it is impossible to determine whether LAN equipment should be regarded as an ADP machine purely on the basis of the ordinary meaning of the terms used in Schedule LXXX taken in isolation. However, as noted above, the meaning of the term "ADP machines" in this context may be determined in light of the legitimate expectations of an exporting Member.<sup>184</sup>

77. In support of this finding, the Panel explained that:

The meaning of a particular expression in a tariff schedule cannot be determined in isolation from its context. It has to be interpreted in the context of Article II of GATT 1994 ... It should be noted in this regard that the protection of legitimate expectations in respect of tariff treatment of a bound item is one of the most important functions of Article II.<sup>185</sup>

The Panel justified this latter statement by relying on the panel report in *European Economic Community - Payments and Subsidies Paid to Processors and Producers of Oilseeds and Related Animal-Feed Proteins*<sup>186</sup> ("*EEC - Oilseeds*"), and stated that:

The fact that the *Oilseeds* panel report concerns a non-violation complaint does not affect the validity of this reasoning in cases where an actual violation of tariff commitments is alleged. If anything, such a direct violation would involve a situation where expectations concerning tariff concessions were even more firmly grounded.<sup>187</sup>

78. The Panel also relied on Article II:5 of the GATT 1994, and stated that:

Although Article II:5 is a provision for the special bilateral procedure regarding tariff classification, not directly at issue in

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<sup>183</sup>See Panel Report, para. 5.15.

<sup>184</sup>Panel Report, para. 8.31.

<sup>185</sup>Panel Report, para. 8.23.

<sup>186</sup>Adopted 25 January 1990, BISD 37S/86, para. 148.

<sup>187</sup>Panel Report, para. 8.23.

this case, the existence of this provision confirms that legitimate expectations are a vital element in the interpretation of Article II and tariff schedules.<sup>188</sup>

79. Finally, the Panel observed that its proposition that the terms of a Member's Schedule may be determined in the light of the "legitimate expectations" of an exporting Member:

... is also supported by the object and purpose of the WTO Agreement and those of GATT 1994. The security and predictability of "the reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade" (expression common in the preambles to the two agreements) cannot be maintained without protection of such legitimate expectations. This is consistent with the principle of good faith interpretation under Article 31 of the Vienna Convention.<sup>189</sup>

80. We disagree with the Panel's conclusion that the meaning of a tariff concession in a Member's Schedule may be determined in the light of the "legitimate expectations" of an exporting Member. First, we fail to see the relevance of the *EEC - Oilseeds* panel report with respect to the interpretation of a Member's Schedule in the context of a violation complaint made under Article XXIII:1(a) of the GATT 1994. The *EEC - Oilseeds* panel report dealt with a non-violation complaint under Article XXIII:1(b) of the GATT 1994, and is not legally relevant to the case before us. Article XXIII:1 of the GATT 1994 provides for three legally-distinct causes of action on which a Member may base a complaint; it distinguishes between so-called *violation* complaints, *non-violation* complaints and *situation* complaints under paragraphs (a), (b) and (c). The concept of "reasonable expectations", which the Panel refers to as "legitimate expectations", is a concept that was developed in the context of *non-violation* complaints.<sup>190</sup> As we stated in *India - Patents*, for the Panel to use this concept in the context of a violation complaint "melds the legally-distinct bases for 'violation' and 'non-violation' complaints under Article XXIII of the GATT 1994 into one uniform cause of action"<sup>191</sup>, and is not in accordance with established GATT practice.

81. Second, we reject the Panel's view that Article II:5 of the GATT 1994 confirms that "legitimate expectations are a vital element in the interpretation" of Article II:1 of the GATT 1994 and of Members' Schedules.<sup>192</sup> It is clear from the wording of Article II:5 that it does not support the Panel's view. This paragraph recognizes the possibility that the treatment *contemplated* in a concession, provided for in a Member's Schedule, on a particular product, may differ from the treatment *accorded* to that product and provides for a compensatory mechanism to rebalance the concessions between the two Members concerned in such a situation. However, nothing in Article II:5 suggests that the expectations of *only* the exporting Member can be the basis for interpreting a concession in a Member's Schedule for the purposes of determining

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<sup>188</sup>Panel Report, para. 8.24.

<sup>189</sup>Panel Report, para. 8.25.

<sup>190</sup>See Appellate Body Report, *India - Patents*, adopted 16 January 1998, WT/DS50/AB/R, paras. 36 and 41.

<sup>191</sup>Adopted 16 January 1998, WT/DS50/AB/R, para. 42.

<sup>192</sup>See Panel Report, para. 8.24.

whether that Member has acted consistently with its obligations under Article II:1. In discussing Article II:5, the Panel overlooked the second sentence of that provision, which clarifies that the "contemplated treatment" referred to in that provision is the treatment contemplated by *both* Members.

82. Third, we agree with the Panel that the security and predictability of "the reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade" is an object and purpose of the *WTO Agreement*, generally, as well as of the GATT 1994.<sup>193</sup> However, we disagree with the Panel that the maintenance of the security and predictability of tariff concessions allows the interpretation of a concession in the light of the "legitimate expectations" of exporting Members, i.e., their *subjective* views as to what the agreement reached during tariff negotiations was. The security and predictability of tariff concessions would be seriously undermined if the concessions in Members' Schedules were to be interpreted on the basis of the subjective views of certain exporting Members alone. Article II:1 of the GATT 1994 ensures the maintenance of the security and predictability of tariff concessions by requiring that Members not accord treatment less favourable to the commerce of *other* Members than that provided for in their Schedules.

83. Furthermore, we do not agree with the Panel that interpreting the meaning of a concession in a Member's Schedule in the light of the "legitimate expectations" of exporting Members is consistent with the principle of good faith interpretation under Article 31 of the *Vienna Convention*. Recently, in *India - Patents*, the panel stated that good faith interpretation under Article 31 required "the protection of legitimate expectations".<sup>194</sup> We found that the panel had misapplied Article 31 of the *Vienna Convention* and stated that:

The duty of a treaty interpreter is to examine the words of the treaty to determine the intentions of the parties. This should be done in accordance with the principles of treaty interpretation set out in Article 31 of the *Vienna Convention*. But these principles of interpretation neither require nor condone the imputation into a treaty of words that are not there or the importation into a treaty of concepts that were not intended.<sup>195</sup>

84. The purpose of treaty interpretation under Article 31 of the *Vienna Convention* is to ascertain the *common* intentions of the parties. These *common* intentions cannot be ascertained on the basis of the subjective and unilaterally determined "expectations" of *one* of the parties to a treaty. Tariff concessions provided for in a Member's Schedule -- the interpretation of which is at issue here -- are reciprocal and result from a mutually-advantageous negotiation between importing and exporting Members. A Schedule is made an integral part of the GATT 1994 by Article II:7 of the GATT 1994. Therefore, the concessions provided for in that Schedule are part of the terms of the treaty. As such, the only rules which may be applied in interpreting the meaning of a concession are the general rules of treaty interpretation set out in the *Vienna Convention*.

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<sup>193</sup>See Panel Report, para. 8.25.

<sup>194</sup>Panel Report, *India - Patents*, adopted 16 January 1998, WT/DS50/R, para. 7.18.

<sup>195</sup>Appellate Body Report, *India - Patents*, adopted 16 January 1998, WT/DS50/AB/R, para. 45.

85. Pursuant to Article 31(1) of the *Vienna Convention*, the meaning of a term of a treaty is to be determined in accordance with the ordinary meaning to be given to this term in its context and in the light of the object and purpose of the treaty. Article 31(2) of the *Vienna Convention* stipulates that:

The context, for the purpose of the interpretation of a treaty shall comprise, in addition to the text, including its preamble and annexes:

- (a) any agreement relating to the treaty which was made between all the parties in connexion with the conclusion of the treaty;
- (b) any instrument which was made by one or more parties in connexion with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.

Furthermore, Article 31(3) provides that:

There shall be taken into account together with the context:

- (a) any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions;
- (b) any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation;
- (c) any relevant rules of international law applicable in the relations between the parties.

Finally, Article 31(4) of the *Vienna Convention* stipulates that:

A special meaning shall be given to a term if it is established that the parties so intended.

86. The application of these rules in Article 31 of the *Vienna Convention* will usually allow a treaty interpreter to establish the meaning of a term.<sup>196</sup> However, if after applying Article 31 the meaning of the term remains ambiguous or obscure, or leads to a result which is manifestly absurd or unreasonable, Article 32 allows a treaty interpreter to have recourse to:

... supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion.

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<sup>196</sup>R. Jennings and A. Watts (eds.), *Oppenheim's International Law*, 9th ed., Vol. I (Longman, 1992), p. 1275.

With regard to "the circumstances of [the] conclusion" of a treaty, this permits, in appropriate cases, the examination of the historical background against which the treaty was negotiated.<sup>197</sup>

87. In paragraphs 8.20 and 8.21 of the Panel Report, the Panel quoted Articles 31 and 32 of the *Vienna Convention* and explicitly recognized that these fundamental rules of treaty interpretation applied "in determining whether the tariff treatment of LAN equipment ... is in conformity with the tariff commitments contained in Schedule LXXX".<sup>198</sup> As we have already noted above, the Panel, after a textual analysis<sup>199</sup>, came to the conclusion that:

... for the purposes of Article II:1, it is impossible to determine whether LAN equipment should be regarded as an ADP machine purely on the basis of the ordinary meaning of the terms used in Schedule LXXX taken in isolation.<sup>200</sup>

Subsequently, the Panel abandoned its effort to interpret the terms of Schedule LXXX in accordance with Articles 31 and 32 of the *Vienna Convention*.<sup>201</sup> In doing this, the Panel erred.

88. As already discussed above, the Panel referred to the *context* of Schedule LXXX<sup>202</sup> as well as to the *object and purpose* of the *WTO Agreement* and the GATT 1994, of which Schedule LXXX is an integral part.<sup>203</sup> However, it did so to support its proposition that the terms of a Schedule may be interpreted in the light of the "legitimate expectations" of an exporting Member. The Panel failed to examine the context of Schedule LXXX and the object and purpose of the *WTO Agreement* and the GATT 1994 in accordance with the rules of treaty interpretation set out in the *Vienna Convention*.

89. We are puzzled by the fact that the Panel, in its effort to interpret the terms of Schedule LXXX, did not consider the *Harmonized System* and its *Explanatory Notes*. We note that during the Uruguay Round negotiations, both the European Communities and the United States were parties to the *Harmonized System*. Furthermore, it appears to be undisputed that the Uruguay Round tariff negotiations were held on the basis of the *Harmonized System's* nomenclature and that requests for, and offers of, concessions were normally made in terms of this nomenclature. Neither the European Communities nor the United States argued before the Panel<sup>204</sup> that the *Harmonized System* and its *Explanatory Notes* were relevant in the interpretation

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<sup>197</sup>I. Sinclair, *The Vienna Convention on the Law of Treaties*, 2nd ed., (Manchester University Press, 1984), p. 141:

... the reference in Article 32 of the Convention to the circumstances of the conclusion of a treaty may have some value in emphasising the need for the interpreter to bear constantly in mind the historical background against which the treaty has been negotiated.

<sup>198</sup>Panel Report, para. 8.22.

<sup>199</sup>See Panel Report, para. 8.30.

<sup>200</sup>Panel Report, para. 8.31.

<sup>201</sup>As discussed above in paragraphs 76-84, the Panel relied instead on the concept of "legitimate expectations" as a means of treaty interpretation.

<sup>202</sup>See Panel Report, paras. 8.23-8.24.

<sup>203</sup>See Panel Report, para. 8.25.

<sup>204</sup>We recall, however, that in reply to our questions at the oral hearing, both the European Communities and the United States accepted the relevance of the *Harmonized System* and its *Explanatory Notes* in interpreting the tariff concessions of Schedule LXXX. See paras. 13 and 38 of this Report.

of the terms of Schedule LXXX. We believe, however, that a proper interpretation of Schedule LXXX should have included an examination of the *Harmonized System* and its *Explanatory Notes*.

90. A proper interpretation also would have included an examination of the existence and relevance of subsequent practice. We note that the United States referred, before the Panel, to the decisions taken by the Harmonized System Committee of the WCO in April 1997 on the classification of certain LAN equipment as ADP machines.<sup>205</sup> Singapore, a third party in the panel proceedings, also referred to these decisions.<sup>206</sup> The European Communities observed that it had introduced reservations with regard to these decisions and that, even if they were to become final as they stood, they would not affect the outcome of the present dispute for two reasons: first, because these decisions could not confirm that LAN equipment was classified as ADP machines in 1993 and 1994; and, second, because this dispute "was about duty treatment and not about product classification".<sup>207</sup> We note that the United States agrees with the European Communities that this dispute is not a dispute on the *correct* classification of LAN equipment, but a dispute on whether the tariff treatment accorded to LAN equipment was less favourable than that provided for in Schedule LXXX.<sup>208</sup> However, we consider that in interpreting the tariff concessions in Schedule LXXX, decisions of the WCO may be relevant; and, therefore, they should have been examined by the Panel.

91. We note that the European Communities stated that the question whether LAN equipment was bound as ADP machines, under headings 84.71 and 84.73, or as telecommunications equipment, under heading 85.17, was *not* addressed during the Uruguay Round tariff negotiations with the United States.<sup>209</sup> We also note that the United States asserted that:

In many, perhaps most, cases, the detailed product composition of tariff commitments was *never* discussed in detail during the tariff negotiations of the Uruguay Round ...<sup>210</sup> (emphasis added)

and that:

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<sup>205</sup>See Panel Report, para. 5.12.

<sup>206</sup>As noted in para. 6.34 of the Panel Report, Singapore pointed out, before the Panel, that:

... the WCO's HS Committee had recently decided that LAN equipment was properly classifiable in heading 84.71 of the HS. The HS Committee had specifically declined to adopt the position advanced that heading 85.17 was the appropriate category ... The EC had suggested that the HS Committee decision was intended solely to establish the appropriate HS classification for future imports. It ignored that the language interpreted by the HS Committee was the same language appearing in the EC's HS nomenclature and in the EC's concession schedule at the time of the negotiations and afterwards.

<sup>207</sup>Panel Report, para. 5.13.

<sup>208</sup>See Panel Report, para. 5.3.

<sup>209</sup>See Panel Report, para. 5.28.

<sup>210</sup>Appellee's submission of the United States, para. 26.

The US-EC negotiation on Chapter 84 provided an example of how two groups of busy negotiators dealing with billions of dollars of trade and hundreds of tariff lines relied on a *continuation of the status quo*.<sup>211</sup> (emphasis added)

This may well be correct and, in any case, seems central to the position of the United States. Therefore, we are surprised that the Panel did not examine whether, during the Tokyo Round tariff negotiations, the European Communities bound LAN equipment as ADP machines or as telecommunications equipment.<sup>212</sup>

92. Albeit, with the mistaken aim of establishing whether the United States "was entitled to legitimate expectations"<sup>213</sup> regarding the tariff treatment of LAN equipment by the European Communities, the Panel examined, in paragraphs 8.35 to 8.44 of the Panel Report, the classification practice regarding LAN equipment in the European Communities during the Uruguay Round tariff negotiations. The Panel did this on the basis of certain BTIs and other decisions relating to the customs classification of LAN equipment, issued by customs authorities in the European Communities during the Uruguay Round.<sup>214</sup> In the light of our observations on "the circumstances of [the] conclusion" of a treaty as a supplementary means of interpretation under Article 32 of the *Vienna Convention*<sup>215</sup>, we consider that the classification practice in the European Communities during the Uruguay Round is part of "the circumstances of [the] conclusion" of the *WTO Agreement* and may be used as a supplementary means of interpretation within the meaning of Article 32 of the *Vienna Convention*. However, two important observations must be made: first, the Panel did *not* examine the classification practice in the European Communities during the Uruguay Round negotiations *as a supplementary means of interpretation* within the meaning of Article 32 of the *Vienna Convention*<sup>216</sup>; and, second, the value of the classification practice as a supplementary means of interpretation is subject to certain qualifications discussed below.

93. We note that the Panel examined the classification practice of only the European Communities<sup>217</sup>, and found that the classification of LAN equipment by the United States during the Uruguay Round tariff negotiations was not relevant.<sup>218</sup> The purpose of treaty interpretation is to establish the *common* intention of the parties to the treaty. To establish this intention, the prior practice of only *one* of the parties may be relevant, but it is clearly of more limited value than the practice of all parties. In the specific case of the interpretation of a tariff concession in a Schedule, the classification practice of the importing Member, in fact, may be of great importance. However, the Panel was mistaken in finding that the classification practice of the United States was *not* relevant.

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<sup>211</sup>Panel Report, para. 5.31.

<sup>212</sup>We note that in paragraph 8 of its third participant's submission, Japan stated that: "[i]n particular, the classification of the LAN equipment among the Members of the EC was not identical before the Uruguay Round".

<sup>213</sup>Panel Report, para. 8.60.

<sup>214</sup>The lists of the BTIs and classification decisions in the form of a letter, submitted by the parties and considered by the Panel, were attached to the Panel Report as Annex 4 and Annex 6 thereof.

<sup>215</sup>See para. 86 of this Report.

<sup>216</sup>It examined the actual classification practice to determine whether the United States could have "legitimate expectations" with regard to the tariff treatment of LAN equipment.

<sup>217</sup>See Panel Report, paras. 8.36-8.44.

<sup>218</sup>See Panel Report, para. 8.60. We note that in paragraph 8.58 of the Panel Report, the Panel stated that the classification of LAN equipment by other WTO Members was not relevant either.

94. In this context, we also note that while the Panel examined the classification practice during the Uruguay Round negotiations, it did not consider the EC legislation on customs classification of goods that was applicable at that time. In particular, it did not consider the "General Rules for the Interpretation of the Combined Nomenclature" as set out in Council Regulation 2658/87 on the Common Customs Tariff.<sup>219</sup> If the classification practice of the importing Member at the time of the tariff negotiations is relevant in interpreting tariff concessions in a Member's Schedule, surely that Member's legislation on customs classification at that time is also relevant.

95. Then there is the question of the *consistency* of prior practice. Consistent prior classification practice may often be significant. Inconsistent classification practice, however, *cannot* be relevant in interpreting the meaning of a tariff concession. We note that the Panel, on the basis of evidence relating to *only* five out of the then 12 Member States<sup>220</sup>, made the following factual findings with regard to the classification practice in the European Communities:

To rebut the presumption raised by the United States, the European Communities has produced documents which *indicate* that LAN equipment had been treated as telecommunication apparatus by other customs authorities in the European Communities.<sup>221</sup> (emphasis added)

... it would be reasonable to conclude at least that the practice [regarding classification of LAN equipment] was not uniform in France during the Uruguay Round.<sup>222</sup>

Germany appears to have consistently treated LAN equipment as telecommunication apparatus.<sup>223</sup>

... LAN equipment was *generally* treated as ADP machines in Ireland and the United Kingdom during the Uruguay Round.<sup>224</sup> (emphasis added)

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<sup>219</sup>Title I, Part I of Annex I of Council Regulation (EEC) No. 2658/87 of 23 July 1987, Official Journal No. L 256, 7 September 1987, p. 1.

<sup>220</sup>With regard to the manner in which the Panel evaluated the evidence regarding classification practice during the Uruguay Round tariff negotiations, we note that in paragraph 8.37 of the Panel Report, the Panel accepted certain BTIs submitted by the United States as relevant evidence, while in footnote 152 of the Panel Report, it considered similar BTIs submitted by the European Communities to be irrelevant.

<sup>221</sup>Panel Report, para. 8.40.

<sup>222</sup>Panel Report, para. 8.42.

<sup>223</sup>Panel Report, para. 8.43.

<sup>224</sup>Panel Report, para. 8.41. In this paragraph, the Panel stated that the only direct counter-evidence against the claim of the United States that customs authorities in Ireland and the United Kingdom consistently classified LAN equipment as ADP machines during the Uruguay Round negotiations is a BTI issued by the UK customs authority to CISCO, classifying one type of LAN equipment (routers) as telecommunications apparatus. The Panel dismisses the value of this BTI as evidence on the basis that it "became effective only a week or so before the conclusion of the Uruguay Round negotiations [15 December 1993]". Similarly, in footnote 152 of the Panel Report, the Panel did not consider other BTIs issued by the UK customs authorities to be relevant because they became valid after the conclusion of the Uruguay Round negotiations. We note, however, that all of these BTIs became valid in December 1993 or February 1994, i.e., before the end of the verification process, to which all Schedules were submitted and which took place

As a matter of logic, these factual findings of the Panel lead to the conclusion that, during the Uruguay Round tariff negotiations, the practice regarding the classification of LAN equipment by customs authorities throughout the European Communities was *not* consistent.

96. We also note that in paragraphs 8.44 and 8.60 of the Panel Report, the Panel identified Ireland and the United Kingdom as the "largest" and "major" market for LAN equipment exported from the United States. On the basis of this assumption, the Panel gave special importance to the classification practice by customs authorities in these two Member States. However, the European Communities constitutes a customs union, and as such, once goods are imported into any Member State, they circulate freely within the territory of the entire customs union. The export market, therefore, is the European Communities, not an individual Member State.

97. For the reasons set out above, we conclude that the Panel erred in finding that the "legitimate expectations" of an exporting Member are relevant for the purposes of interpreting the terms of Schedule LXXX and of determining whether the European Communities violated Article II:1 of the GATT 1994. We also conclude that the Panel misinterpreted Article II:5 of the GATT 1994.

98. On the basis of the erroneous legal reasoning developed and the selective evidence considered, the Panel was not justified in coming to the conclusion that the United States was entitled to "legitimate expectations" that LAN equipment would be accorded tariff treatment as ADP machines in the European Communities<sup>225</sup> and, therefore, that the European Communities acted inconsistently with the requirements of Article II:1 of the GATT 1994 by failing to accord imports of LAN equipment from the United States treatment no less favourable than that provided for in Schedule LXXX.<sup>226</sup>

99. In the light of our conclusion that the "legitimate expectations" of an exporting Member are not relevant in determining whether the European Communities violated Article II:1 of the GATT 1994, we see no reason to examine the subordinate claim of error of the European Communities relating to the evidence on which the "legitimate expectations" of exporting Members were based.

## **VI. Clarification of the Scope of Tariff Concessions**

100. The last issue raised by the European Communities in this appeal is whether the Panel erred in placing the onus of clarifying the scope of a tariff concession during a multilateral tariff negotiation, held under the auspices of the GATT/WTO, solely on the importing Member.

101. In paragraph 8.60 of the Panel Report, the Panel concluded that:

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between 15 February 1994 and 25 March 1994 (MTN.TNC/W/131, 21 January 1994). Therefore, in our view, the Panel should have considered these BTIs.

<sup>225</sup>See Panel Report, para. 8.60.

<sup>226</sup>See Panel Report, para. 9.1.

We find that the United States was entitled to legitimate expectations that LAN equipment would continue to be accorded tariff treatment as ADP machines in the European Communities, based on the actual tariff treatment during the Uruguay Round, particularly in Ireland and the United Kingdom ... We further find that the United States was not required to *clarify the scope* of the European Communities' *tariff concessions* on LAN equipment ... (emphasis added)

Prior to this conclusion, the Panel stated the following:

... we find that the European Communities cannot place the burden of clarification on the United States in cases where it has created, through its own practice, the expectations regarding the continuation of the actual tariff treatment prevailing at the time of the tariff negotiations. It would not be reasonable to expect the US Government to seek clarification when it had not heard any complaints from its exporters, who were apparently satisfied with the current tariff treatment of LAN equipment in their major export market -- Ireland and the United Kingdom.<sup>227</sup>

102. The European Communities appeals these findings, and argues that:

... the Panel erred where it considered that, in any case, the onus of clarifying the scope of a tariff concession during a multilateral tariff negotiation ... shall necessarily be put on the side of the importing Member. By doing so, the Panel has created and applied a new rule on the burden of proof in the dispute settlement procedure which is outside its terms of reference and is beyond the powers of a panel.<sup>228</sup>

103. We do not agree that the Panel has created and applied a new rule on the burden of proof. The rules on the burden of proof are those which we clarified in *United States - Shirts and Blouses*.<sup>229</sup>

104. The Panel's findings in paragraphs 8.55 and 8.60 on the "requirement of clarification" are linked to the Panel's reliance on "legitimate expectations" as a means of interpretation of the tariff concessions in Schedule LXXX. They serve to complete and buttress the Panel's conclusion that "the United States was entitled to legitimate expectations that LAN

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<sup>227</sup>Panel Report, para. 8.55.

<sup>228</sup>Notice of Appeal of the European Communities, para. 4.

<sup>229</sup>Adopted 23 May 1997, WT/DS33/AB/R, p. 14. See also, Appellate Body Report, *EC Measures Concerning Meat and Meat Products (Hormones)*, adopted 13 February 1998, WT/DS26/AB/R, WT/DS48/AB/R, paras. 97-109.

equipment would continue to be accorded tariff treatment as ADP machines in the European Communities".<sup>230</sup>

105. We note that the Panel's findings in paragraphs 8.55 and 8.60 on the "requirement of clarification" were, in fact, the Panel's response to the question whether:

... the exporting Member has any inherent obligation to seek clarification when it has been otherwise given a basis to expect that actual tariff treatment by the importing Member will be maintained.<sup>231</sup>

106. We also note the Panel's references<sup>232</sup> to the panel report in *Panel on Newsprint* and the report by the Group of Experts in *Greek Increase in Bound Duty*.<sup>233</sup> In both of these reports, the conclusions on the obligations of the importing contracting party under Article II:1 of the GATT 1994 were reached on the basis of the ordinary meaning of the wording of the respective Schedules. These reports also assume that the tariff concessions made by the importing contracting party would have had to be limited by "conditions or qualifications" if they were to be interpreted restrictively. That the Panel reads these two reports in this way is evident from the Panel's concluding remark that "these cases ... confirm that the onus of clarifying tariff *commitment* is generally placed on the importing Member" (emphasis added).<sup>234</sup>

107. However, the case before us raises a different problem. The question here is whether the European Communities has committed itself to treat LAN equipment as ADP machines under headings 84.71 or 84.73, rather than as telecommunications equipment under heading 85.17 of Schedule LXXX. We do not believe that the "requirement of clarification", as discussed by the Panel, is relevant to this question.

108. The Panel also based its conclusions on the "requirement of clarification" on a certain perception of the nature of tariff commitments. The Panel stated:

... that a tariff commitment is an instrument in the hands of an importing Member which inherently serves the importing

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<sup>230</sup>Panel Report, para. 8.60.

<sup>231</sup>Panel Report, para. 8.48.

<sup>232</sup>See Panel Report, paras. 8.51-8.54.

<sup>233</sup>L/580, 9 November 1956. We note that while the panel report in *Panel on Newsprint* was adopted by the CONTRACTING PARTIES, the report by the Group of Experts in *Greek Increase in Bound Duty* was not.

<sup>234</sup>Panel Report, para. 8.54.

Member's "protection needs and its requirements for the purposes of tariff and trade negotiations". ... It is for this reason that it behooves the importing party, as the effective bearer of its rights and responsibilities, to correctly identify products and relevant duties in its tariff schedules, including such limitations or modifications as it intends to apply.<sup>235</sup>

109. We do not share this perception of the nature of tariff commitments. Tariff negotiations are a process of reciprocal demands and concessions, of "give and take". It is only normal that importing Members define their offers (and their ensuing obligations) in terms which suit their needs. On the other hand, exporting Members have to ensure that their corresponding rights are described in such a manner in the Schedules of importing Members that their export interests, as agreed in the negotiations, are guaranteed. There was a special arrangement made for this in the Uruguay Round. For this purpose, a process of verification of tariff schedules took place from 15 February through 25 March 1994, which allowed Uruguay Round participants to check and control, through consultations with their negotiating partners, the scope and definition of tariff concessions.<sup>236</sup> Indeed, the fact that Members' Schedules are an integral part of the GATT 1994 indicates that, while each Schedule represents the tariff commitments made by *one* Member, they represent a common agreement among *all* Members.

110. For the reasons stated above, we conclude that the Panel erred in finding that "the United States was not required to clarify the scope of the European Communities' tariff concessions on LAN equipment".<sup>237</sup> We consider that any clarification of the scope of tariff concessions that may be required during the negotiations is a task for *all* interested parties.

## **VII. Conclusions**

111. For the reasons set out in this Report, the Appellate Body:

- (a) upholds the finding of the Panel that the request of the United States for the establishment of a panel met the requirements of Article 6.2 of the DSU;
- (b) reverses the findings of the Panel that the United States was entitled to "legitimate expectations" that LAN equipment would be accorded tariff treatment as ADP machines in the European Communities and, therefore, that the European Communities acted inconsistently with the requirements of Article II:1 of the GATT 1994 by failing to accord imports of LAN equipment from the United States treatment no less favourable than that provided for in Schedule LXXX; and
- (c) reverses the ancillary finding of the Panel that the United States was not required to clarify the scope of the European Communities' tariff concessions on LAN equipment.

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<sup>235</sup>Panel Report, para. 8.50.

<sup>236</sup>MTN.TNC/W/131, 21 January 1994. See also *Marrakesh Protocol to the General Agreement on Tariffs and Trade 1994*, para. 3.

<sup>237</sup>Panel Report, para. 8.60.

## **2. The Most Favored Nation Principle**

### 2-1. INTRODUCTION

#### **Relevant Provisions**

Read in the Primary Sources:

- Article I GATT 1994
- Article II GATS

## Origin of the Most-Favored Nation (MFN) Principle

*Excerpt from an OECD working paper on international investment*

<http://www.oecd.org/dataoecd/21/37/33773085.pdf>

(footnotes omitted)

MFN treatment has been a central pillar of trade policy for centuries. It can be traced back to the twelfth century, although the phrase seems to have first appeared in the seventeenth century. MFN treaty clauses spread with the growth of commerce in the fifteenth and sixteenth centuries. The United States included an MFN clause in its first treaty, a 1778 treaty with France. In the 1800s and 1900s the MFN clause was included frequently in various treaties, particularly in the Friendship, Commerce, and Navigation treaties. MFN treatment was made one of the core obligations of commercial policy under the Havana Charter where Members were to undertake the obligation “to give due regard to the desirability of avoiding discrimination as between foreign investors”. The inclusion of MFN clauses became a general practice in the numerous bilateral, regional and multilateral investment-related agreements which were concluded after the Charter failed to come into force in 1950. Its importance for international economic relations is underscored by the fact that the MFN treatment provisions of the GATT (Article I *General Most-Favoured-Nation Treatment*) and the GATS (Article II *Most-Favoured-Nation Treatment*) provide that this obligation shall be accorded “immediately and unconditionally” (although in the case of the GATS, a member may maintain a measure inconsistent with this obligation provided that such measure is listed in, and meets the conditions of, the Annex on Article II Exemptions).

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For a thorough history of the MFN clause up to the Second World War, including the work done by, or under the auspices of, the League of Nations, see the First Report of the ILC’s Special Rapporteur, *Yearbook of the International Law Commission*, 1969, Vol. II, p. 157 ff.

## 2-2. SPANISH COFFEE

*The following two panel reports date from the 1980s and are among the relatively few MFN disputes. Compare the following two GATT panel reports and consider how to legally reconcile them. Focus in particular on the expressly and implicitly applied criteria for the determination of likeness and keep in mind the economic rationale for the MFN obligation.*

*Once again try to understand the market: What was Spain's rationale for introducing a differentiation in their tariff between mild and other coffees?*

*Lawyering Exercise: If at the time Spanish Coffee was decided there had been an Appellate Body and you were Spain's legal counsel -- how would you have phrased the appeal to show that "mild" coffee and "unwashed Arabica" are not like products?*

[http://www.wto.org/english/tratop\\_e/dispu\\_e/gt47ds\\_e.htm](http://www.wto.org/english/tratop_e/dispu_e/gt47ds_e.htm)

27 April 1981

### SPAIN - TARIFF TREATMENT OF UNROASTED COFFEE

*Report of the Panel adopted on 11 June 1981  
(L/5135 - 28S/102)*

#### I. Introduction

1.1 In a communication dated 13 September 1979 and circulated to contracting parties, Brazil informed that a new Spanish law had introduced certain modifications in the tariff treatment applied to imports of unroasted coffee, according to which imports into Spain of unroasted non-decaffeinated "unwashed Arabica" and Robusta coffees (tariff No. 09.01A) were now subject to a tariff treatment less favourable than that accorded to "mild" coffee. Prior to this new law there had been no differentiation in the tariff treatment applied by Spain to imports of unroasted coffee. As a main supplier of coffee to Spain, Brazil was concerned with the discriminatory character of the new tariff rates and had requested Article XXII:1 consultations with Spain (L/4832).

(...)

#### II. Factual aspects

2.1 The following is a brief description of factual aspects of the matter under dispute as the Panel understood them.

2.2 On 8 July 1979, the Spanish authorities enacted the Royal Decree No. 1764/79 (B.O.E. of 20 July) by which the tariff treatment and the sub-tariff classification applied to imports of unroasted, non-decaffeinated coffee (ex. CCCN 09.01) were modified and amended, effective by 1 March 1980. Imports of unroasted coffee, which prior to this last date entered Spain's customs territory under one and the same designation, was sub-divided into five tariff lines to which duty rates applied as follows:

Table 1

Spain's present tariff treatment for unroasted non-decaffeinated coffee beans  
(Royal Decree 1764/79 - Tariff No. 09.01. A.1a)

Product description	Duty rate
1. Columbian mild	Free
2. Other mild	Free
3. Unwashed Arabica	7 per cent ad. val.
4. Robusta	7 per cent ad. val.
5. Other	7 per cent ad. val.

2.3 Prior to the Royal Decree 1764/79, imports of unroasted coffee into Spain were subject to a customs duty of 25 per cent ad valorem<sup>1</sup>, which was subsequently reduced to 22.5 per cent. In 1975, by Decree-Law 13/75 of 17 November of that year, Spain exempted imports of certain food products, including unroasted coffee, from customs duties when they were imported under the State-trading system.

2.4 Ever since Spain acceded to GATT, customs duties on raw coffee were never bound, and, therefore, not included in Schedule XLV of Spanish concessions in GATT.

2.5 On the same date, 8 July 1979, the Spanish authorities also published the Royal Decree 1765/79 which provided that as from 1 March 1980 imports of unroasted coffee would cease to be under State-trading and would begin to be marketed by private entities. Prior to that, imports of unroasted coffee into Spain were the monopoly of the Office of the General Commissioner for Supply and Transport (CAT) which also had exclusive responsibility for domestic supply.

2.6 Under the State-trading régime and intervention in the domestic market, the use of blends was prohibited in Spain and coffee was obligatorily marketed under the designations Superior, Regular and Popular, which largely corresponded to the types "mild", "unwashed Arabica", and Robusta, respectively. The CAT also maintained a system of maximum authorized prices for each of these types of coffee.

<sup>1</sup>Decree 999/60 of 30 May 1960.

2.7 On 30 November 1979, a Ministerial Order (Ministry of Trade and Tourism) did away with the requirement to market coffee under the designations Superior, Regular and Popular. Confirming this removal of obligatory designations, the Resolution of the same Ministry's General Directorate of Domestic Trade, of 8 February 1980, indicated a single maximum price for the domestic sale of these products without distinction as to type.

2.8 This latter resolution having also been superseded, the Panel further understood that, at the present time, domestic coffee prices were free in the Spanish market.

2.9 Spain's imports of raw coffee clearly showed a rising trend over the period 1967-1979 having increased two-fold by volume, and ten-fold by value.

Table 2

Spain's Imports of Raw Coffee  
(Tariff No. 09.01.A.1 and Statistical No. 09.01.01)

Year	Metric tons	Million pts.	Main suppliers
1967	42,215	2,378	Colombia, <u>Brazil</u> , Mexico, Angola
1968	49,075	2,997	Colombia, <u>Brazil</u> , Angola, Mexico
1969	61,877	3,767	Colombia, <u>Brazil</u> , Angola, Mexico
1970	78,963	5,747	Colombia, <u>Brazil</u> , Angola, Uganda
1971	66,353	4,916	Colombia, <u>Brazil</u> , Angola, Mexico
1972	80,239	5,786	Colombia, <u>Brazil</u> , Angola, Equatorial Guinea
1973	73,464	5,789	<u>Brazil</u> , Colombia, Angola, Mexico
1974	84,898	7,215	Colombia, <u>Brazil</u> , Angola, Mexico
1975	75,788	6,325	Colombia, Angola, Ivory Coast, <u>Brazil</u>
1976	91,698	13,765	<u>Brazil</u> , Ivory Coast, Uganda, Colombia
1977	77,479	31,693	<u>Brazil</u> , Ivory Coast, Colombia, Uganda
1978	83,226	24,452	Colombia, <u>Brazil</u> , El Salvador, Ivory Coast
1979	99,621	22,291	Colombia, Uganda, <u>Brazil</u> , Ivory Coast

Source: Foreign Trade Statistics of Spain - General Directorate of Customs.

Note: The above figures cover only imports into the Peninsula and the Balearic Islands and exclude imports into Free Zones.

2.10 The increases in value and volume were not parallel, owing not only to international market fluctuations but also to differences in the composition of the Spanish imports, in terms of types of coffee. While varying, the main suppliers always included both Brazil and Colombia, although neither was always the principal supplier.

2.11 Spain's imports of unroasted coffee from Brazil were constituted of almost entirely "unwashed Arabica", and they evolved in most recent times as shown by Table 3.

Table 3

Spain's Imports of Raw Coffee (metric tons)

	1976	1977	1978	1979	March-September 1980
Total	91,698	77,749	83,226	99,621	74,668
of which from Brazil:	40,672	24,946	18,137	18,573	21,004
% of total	44.35	32.08	21.69	18.64	28.13

Source: see Table 2.

### III. Main arguments

#### Article I:1

3.1 The representative of Brazil argued that by introducing a 7 per cent tariff rate on imports of unroasted, non-decaffeinated coffee of the "unwashed Arabica" and Robusta groups, while affording duty-free treatment to coffee of other groups, the new Spanish tariff régime was discriminatory against Brazil, which exports mainly "unwashed Arabica", but also Robusta coffee, and therefore was in violation of Article I:1 of the General Agreement, according to which:

"... any advantage, favour, privilege or immunity granted by any contracting party to any product originating in ... any other country shall be accorded immediately and unconditionally to the like product originating in ... the territories of all other contracting parties."

3.2 In this connection, he noted that, as did Spain herself under her previous tariff régime, no other contracting party discriminated in its customs tariff as between "types" or as among "groups" of coffee.

3.3 The representative of Spain, stressed that no contracting party was obliged to retain either its tariff structure, or its duties, applicable to the importation of products which have not been bound. He recalled that the Brussels nomenclature adopted by Spain did specify tariff headings but left it to each country to establish, if it is so wished, sub-headings within these headings. Accordingly, the Spanish authorities had the right to establish within a given heading the sub-divisions which were most suited to the characteristics of Spain's foreign trade, while respecting, as Spain has done on many occasions, the bound duties previously negotiated.<sup>1</sup> The classification criterion adopted was based on classifications made by international organizations, specifically the International Coffee Organization (ICO).

3.4 In order to ascertain the coverage of Article I:1 it was necessary, in the view of the Spanish representative, to consider two aspects in detail: (a) meaning of the term "like products", and (b) existence of any preference or pretermission in respect of a country as a consequence of the new structure of heading No. 09.01.A.1 of the Spanish tariff. The Spanish authorities continued to hold that, in their judgment, the provisions of the Royal Decree 1764/79 were fully compatible with the obligations assumed by Spain under the General Agreement, and in particular Article I:1 thereof.

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<sup>1</sup>In this respect, the representative of Brazil requested the Panel to take note of the oral recognition made by the Spanish representative in the course of the first hearing of the Panel that Article I of GATT applied equally to bound and unbound tariff items.

These authorities furnished photocopies of importing licences in Spain, issued after 1 March 1980, which evidenced that the new tariff classification was applied according to the nature of products, and completely independently of the country of origin. In particular, these licences evidenced that Brazilian "washed" coffee was imported into Spain free of duty.

"Like products"

3.5 Recalling that in some past GATT cases it had been suggested that "like products" were all the products falling within the same tariff heading, the representative of Spain did not agree with that opinion. In his view, this interpretation could lead to serious mistakes, given that products falling within one and the same tariff heading could be unlike and clearly different, as for example: (i) in the case of all the residual tariff headings ("other products not specified"), covering a large number of heterogeneous products, and (ii) headings including homogeneous products where in many instances these were not "like products" (i.e. CCCN heading No. 15.07 including all kinds of vegetable oils; CCCN heading No. 22.05 including all wines, etc.).

3.6 The Spanish representative pointed out that qualitative differences did exist between various types of coffee considering both technico-agronomic, economic and commercial criteria. He argued that Robusta coffee bean was morphologically different from the Arabica coffee bean, having a different chemical composition and yielding a neutral beverage that was lacking in aroma and was richer in soluble solids than the beverage made from Arabica coffee.

3.7 Although both "mild" and "unwashed Arabica" coffees belonged to the group of Arabica, the Spanish representative further argued that differences in quality also existed between them, as a result of climatic and growing conditions as well as methods of cultivation and above all the preparation because aroma and taste, essential features in determining trade and consumption of these products, were completely different in "washed" and "unwashed" Arabica coffees. Different quotations in international trade and commodity markets were due to these factors.

3.8 As distinctive markets existed for the various types of unroasted coffee, the Spanish representative was of the view that such various types of coffee could not be regarded as "like products". This was particularly evident in the Spanish market where, for historical reasons, consumers' preference for the various types of coffee was well established, in contrast with other markets in which the use of blends was more generalized. When referring to the increasing market share of blends outside Spain, he argued that the existence of blends proved that the various types of coffee were not the same products.

3.9 For his part, the representative of Brazil argued that coffee was one single product and that, therefore, for the purpose of Article I:1 of the GATT, must be considered a "like product". He further argued that in the specific case of "mild" and "unwashed Arabica" coffees, both came from the same species of plant, and often from the same variety of tree. He also stated that, in such cases, the product could be extracted from the same individual tree, and the classification as "unwashed Arabica" or "mild" would depend exclusively on the treatment given to the berries.

3.10 He pointed out, therefore, that existing differences between "growths" or "groups" of coffee were essentially of an organoleptic nature (taste, aroma, body, etc.) resulting from geographical conditions and, principally, from the distinct methods of preparation of the beans.

3.11 He stated that the classification presently used by Spain for tariff purposes had been introduced by the International Coffee Organization in 1965/66, when the Council of the Organization decided to create groupings of coffee-producing countries as part of a system for the limited adjustment of export quotas in response to changes in an indicator price of "mild Arabicas", "unwashed Arabicas" and "Robustas". He further stated that the composition of each grouping depended upon political decisions taken yearly by the Council of the Organization, according to which each exporting country was placed in the group corresponding to the kind of coffee constituting the greater part of its production. He stressed that since 1972 these groupings had only served a statistical purpose.

3.12 He argued that, from the point of view of the consumer, virtually all coffee, either roasted or soluble, was sold today in the form of blends, combining in varying proportions coffee belonging to different groups. Moreover, in everyday language, the terms type, quality, and growth were used interchangeably to indicate specific grades of coffee, for instance Colombian Mams, El Salvador Central Standard, Paranà 4, Angola Ambriz 2AA, etc. In his view, this was the only characterization really meaningful for trading purposes, since no roaster did buy a "Colombian mild" or "unwashed Arabica" as such, but rather well-known grades, priced according to the beverage they could provide.

3.13 He further stated that with respect to its end use, coffee was a well determined and one single product, generally intended for drinking as a beverage.

#### Differentiation made in the Spanish tariff

3.14 Explaining the economic reasons beyond the differentiation introduced in the Spanish tariff by the Royal Decree No. 1764/79, the representative of Spain said that the lower customs duty applicable to "mild" coffee imported into Spain reflected the Spanish Government's deep concern over the possible impact on prices of measures to return coffee to the private sector and afford greater trade liberalization. In this connection, he noted that coffee accounted for more than 2 per cent in the Spanish consumer price index. He also said that in the previous trade system of State-trading in which a nil tariff duty existed since 1975, nevertheless the difference between import prices and selling prices to roasters ("precios de cesión") in practice constituted an implicit tariff affecting all imports of coffee. This implicit tariff was higher than the tariff duties effectively applied since March 1980.

3.15 Having recalled that a very high proportion of "mild" coffee was consumed in the Spanish market, he noted that this very high proportion of "mild" in Spanish consumption had been maintained by keeping artificially low the retail price of "mild" coffee through the operation of the previously existing system of authorized prices.

3.16 In view of the foregoing, he indicated that his authorities had considered that the only way of reconciling consumers' preference for "mild" coffee and the transfer of the coffee trade to the private sector was to establish different rates of custom duty, with a zero duty on the most expensive coffee, i.e. "mild" coffee. In so doing, his authorities had not at any time given any thought to which countries were producing the different types of coffee. In fact, different types or groups of coffee were often grown in one and the same country and more than thirty countries were producing both Robusta and "unwashed Arabica".

3.17 Finally, the Spanish representative stressed the transitional character of the coffee import régime actually applied by his country. He said that his authorities ultimately aimed, in the shortest possible time, at introducing in respect of coffee a system of automatic licensing and free domestic trade.

3.18 Referring to the stated anti-inflation objective of the Spanish measures, the representative of Brazil was of the view that such argument was not relevant to the case under dispute, since, whatever the motivation to introduce the new tariff régime for unroasted coffee, such motivation did not exempt Spain from complying with the provisions of Article I:1 of the GATT.

(...)

#### IV. Findings and conclusions

4.1 The Panel has carried out its consideration of the matter referred to it for examination in the light of its terms of reference and on the basis of various factual information which was available to it, and of arguments presented to it by the parties to the dispute.

4.2 The Panel considered that it was called upon to examine whether the Spanish tariff régime for unroasted coffee introduced by Spain through the Royal Decree 1764/79 (ref. paragraph 2.2) was consistent with Spanish obligations under the GATT, and more precisely whether it was in conformity with the most-favoured-nation provision of Article I:1.

4.3 Having noted that Spain had not bound under the GATT its tariff rate on unroasted coffee, the Panel pointed out that Article I:1 equally applied to bound and unbound tariff items.

4.4 The Panel found that there was no obligation under the GATT to follow any particular system for classifying goods, and that a contracting party had the right to introduce in its customs tariff new positions or sub-positions as appropriate.<sup>1</sup> The Panel considered, however, that, whatever the classification adopted, Article I:1 required that the same tariff treatment be applied to "like products".

4.5 The Panel, therefore, in accordance with its terms of reference, focused its examination on whether the various types of unroasted coffee listed in the Royal Decree 1764/79 should be regarded as "like products" within the meaning of Article I:1. Having reviewed how the concept of "like products" had been applied by the CONTRACTING PARTIES in previous cases involving, inter alia, a recourse to Article I:1<sup>2</sup> the Panel noted that neither the General Agreement nor the settlement of previous cases gave any definition of such concept.

4.6 The Panel examined all arguments that had been advanced during the proceedings for the justification of a different tariff treatment for various groups and types of unroasted coffee. It noted that these arguments mainly related to organoleptic differences resulting from geographical factors, cultivation methods, the processing of the beans, and the genetic factor. The Panel did not consider that such differences were sufficient reason to allow for a different tariff treatment. It pointed out that it was not unusual in the case of agricultural products that the taste and aroma of the end-product would differ because of one or several of the above-mentioned factors.

4.7 The Panel furthermore found relevant to its examination of the matter that unroasted coffee was mainly, if not exclusively, sold in the form of blends, combining various types of coffee, and that coffee in its end-use, was universally regarded as a well-defined and single product intended for drinking.

4.8 The Panel noted that no other contracting party applied its tariff régime in respect of unroasted, non-decaffeinated coffee in such a way that different types of coffee were subject to different tariff rates.

4.9 In the light of the foregoing, the Panel concluded that unroasted, non-decaffeinated coffee beans listed in the Spanish Customs Tariffs under CCCN 09.01 A.1a, as amended by the Royal Decree 1764/79, should be considered as "like products" within the meaning of Article I:1.

4.10 The Panel further noted that Brazil exported to Spain mainly "unwashed Arabica" and also Robusta coffee which were both presently charged with higher duties than that applied to "mild"

coffee. Since these were considered to be "like products", the Panel concluded that the tariff régime as presently applied by Spain was discriminatory vis-à-vis unroasted coffee originating in Brazil.

4.11 Having recalled that it had found the tariff régime for unroasted coffee introduced by Spain through the Royal Decree 1764/79 not to be in conformity with the provision of Article I:1, the Panel further concluded that this constituted prima facie a case of impairment of benefits accruing to Brazil within the meaning of Article XXIII.

4.12 In the light of the above, the Panel suggest that the CONTRACTING PARTIES request Spain to take the necessary measures in order to make its tariff régime for unroasted coffee conform to Article I:1.

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<sup>1</sup>Provided that a reclassification subsequent to the making of a concession under the GATT would not be a violation of the basic commitment regarding that concession (Article II:5).

<sup>2</sup>BISD Vol. II/188; BISD S1/53; BISD S25/49; L/5047.

## 2-3. JAPAN – LUMBER

*It has been suggested by Robert Hudec that the narrow interpretation by the panel of the “like product” concept in Art. I:1 GATT is consistent with the GATT approach towards tariffs and the structure of tariff negotiations. Think about it.*

[http://www.wto.org/english/tratop\\_e/dispu\\_e/gt47ds\\_e.htm](http://www.wto.org/english/tratop_e/dispu_e/gt47ds_e.htm)

### JAPAN – TARIFF ON IMPORTS OF SPRUCE, PINE, FIR (SPF) DIMENSION LUMBER *Report of the Panel adopted on 19 July 1989*

(L/6470-36S/167)

(...)

#### V. FINDINGS

5.1 Under its terms of reference established by the Council the Panel had to examine a complaint by Canada that the application of a tariff duty of 8 per cent on imports of spruce-pine-fir (SPF) dimension lumber by Japan is not in conformity with the provisions of Article I:1 of the General Agreement and nullifies and impairs benefits accruing to Canada under the General Agreement, SPF dimension lumber being a "like product" as compared to other types of dimension lumber entering Japan with zero duty.

(...)

5.4 According to Canada, Article I:1 required Japan to accord also to SPF dimension lumber the advantage of the zero tariff granted by Japan, under sub-position 4407.10-320 of its Tariff, to planed and sanded lumber of "other" coniferous trees, including the genera cedar and other Chamaecyparis, hemlock (Tsuga), and douglas-fir (Pseudotsuga), and five species excluded from sub-position No. 4407.10-110.

5.5 The Panel noted that the tariff classification for 4407.10-110 had been established autonomously by Japan, without negotiation.

5.6 The terms of Article I:1, as far as they are relevant to the issue, read as follows:

#### General Most-Favoured Nation Treatment

"With respect to customs duties ... imposed on ... imports ... any advantage ... granted by any contracting party to any product originating in ... any other country ... shall be accorded ... to the like product originating in ... all other contracting parties."

5.7 In view of analysing the factual situation submitted to it under its terms of reference, the Panel had first to consider the legal framework in which the Canadian complaint had been raised. In substance, Canada complains of the fact that Japan had arranged its tariff classification in such a way that a considerable part of Canadian exports of SPF dimension lumber to Japan was submitted to a customs duty of 8 per cent, whereas other comparable types of dimension lumber enjoy the advantage of a zero-tariff duty. The Panel considered it impossible to appreciate fully the Canadian

complaint if it had not in a preliminary way clarified the bearing of some principles of the GATT-system in relation to tariff structure and tariff classification.

5.8 The Panel noted in this respect that the General Agreement left wide discretion to the contracting parties in relation to the structure of national tariffs and the classification of goods in the framework of such structure (see the report of the Panel on Tariff Treatment of Unroasted Coffee, BISD 28S/102, at III, paragraph 4.4). The adoption of the Harmonized System, to which both Canada and Japan have adhered, had brought about a large measure of harmonization in the field of customs classification of goods, but this system did not entail any obligation as to the ultimate detail in the respective tariff classifications. Indeed, this nomenclature has been on purpose structured in such a way that it leaves room for further specifications.

5.9 The Panel was of the opinion that, under these conditions, a tariff classification going beyond the Harmonized System's structure is a legitimate means of adapting the tariff scheme to each contracting party's trade policy interests, comprising both its protection needs and its requirements for the purposes of tariff- and trade negotiations. It must however be borne in mind that such differentiations may lend themselves to abuse, insofar as they may serve to circumscribe tariff advantages in such a way that they are conducive to discrimination among like products originating in different contracting parties. A contracting party prejudiced by such action may request therefore that its own exports be treated as "like products" in spite of the fact that they might find themselves excluded by the differentiations retained in the importing country's tariff.

5.10 Tariff differentiation being basically a legitimate means of trade policy, a contracting party which claims to be prejudiced by such practice bears the burden of establishing that such tariff arrangement has been diverted from its normal purpose so as to become a means of discrimination in international trade. Such complaints have to be examined in considering simultaneously the internal protection interest involved in a given tariff specification, as well as its actual or potential influence on the pattern of imports from different extraneous sources. The Canadian complaint and the defence of Japan will have to be viewed in the light of these requirements.

5.11 "Dimension lumber" as understood by Canada is defined by its presentation in a standard form of measurements, quality-grading and finishing. It appears from the information provided by Canada that this type of lumber is largely used in platform-house construction in Canada as well as in the United States and that it has found also widespread use in Japan, as is testified by the existence of a Japanese technical standard known under the name of "JAS 600".

5.12 Japan objected to this claim on different grounds. Japan explained that dimension lumber was only one particular type of lumber among many other possible presentations and that house-building is only one of the many possible uses of this particular kind of lumber. From the legal point of view, Japan contended that the concept of "dimension lumber" is not used either in any internationally accepted tariff classification, or in the Japanese tariff classification. In accordance with the Harmonized System, position No. 4407.10 embraces all types of coniferous wood "sawn or chipped lengthwise ... exceeding 6mm". Apart from the thickness and the grade of finishing, customs treatment of lumber according to the Japanese Tariff was determined exclusively on the basis of a distinction established between certain biological genera or species. Dimension lumber was therefore not identified as a particular category in the framework of the Japanese tariff classification.

5.13 The Panel considered that the tariffs referred to by the General Agreement are, quite evidently, those of the individual contracting parties. This was inherent in the system of the Agreement and appeared also in the current practice of tariff negotiations, the subject matter of which were the national tariffs of the individual contracting parties. It followed that, if a claim of likeness was raised by a contracting party in relation to the tariff treatment of its goods on

importation by some other contracting party, such a claim should be based on the classification of the latter, i.e. the importing country's tariff.

5.14 The Panel noted in this respect that "dimension lumber" as defined by Canada was a concept extraneous to the Japanese Tariff. It was a standard applied by the Canadian industry which appeared to have some equivalent in the United States and in Japan itself, but it could not be considered for that reason alone as a category for tariff classification purposes, nor did it belong to any internationally accepted customs classification. The Panel concluded therefore that reliance by Canada on the concept of dimension lumber was not an appropriate basis for establishing "likeness" of products under Article I:1 of the General Agreement.

5.15 At the same time, the Panel felt unable to examine the Canadian complaint in a broader context, as Canada had declared expressly that the issue before the Panel should not be confused by broadening the scope of the Panel's examination beyond 'dimension lumber' to planed lumber generally. Canada's complaint was limited to the specific product known in North America, and also in Japan, as dimension lumber. Canada did not contend that different lumber species per se should be considered like products, regardless of the product-form they might take (see para. 3.15 above). Thus there appeared to be no basis for examining the issue raised by Canada in the general context of the Japanese tariff classification.

5.16 In these circumstances the Panel was not in a position to pursue further the questions relating to the concept of "like products" in the framework of Article I:1 of the General Agreement.

## VI. CONCLUSIONS

6.1 In the light of the considerations set out in Section V above, the Panel could not establish that the tariff treatment of Canadian dimension lumber applied by Japan under its tariff number 4407.10-110 was inconsistent with Article I:1 of the General Agreement.

## 2-4. EXCEPTIONS

### **Regionalism (cf. Unit 2)**

Art. XXIV GATT and Art. V GATS

### **Enabling Clause for developing countries (goods)**

[http://www.wto.org/english/tratop\\_e/devel\\_e/d2legl\\_e.htm#enabling\\_clause](http://www.wto.org/english/tratop_e/devel_e/d2legl_e.htm#enabling_clause)

[The Enabling Clause](#) (download in MS Word, 2 pages, 38KB) officially called the “Decision on Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries”, was adopted under GATT in 1979 and enables developed members to give differential and more favorable treatment to developing countries.

The Enabling Clause is the WTO legal basis for the **Generalized System of Preferences (GSP)**. Under the Generalized System of Preferences, developed countries offer non-reciprocal preferential treatment (such as zero or low duties on imports) to products originating in developing countries. Preference-giving countries unilaterally determine which countries and which products are included in their schemes.

The Enabling Clause is also the legal basis for [regional arrangements](#) among developing countries and for the **Global System of Trade Preferences (GSTP)**, under which a number of developing countries exchange trade concessions among themselves.

For more information about the GSP and the GSTP, see the [UNCTAD website](#).

### **Text of the Enabling Clause:**

DIFFERENTIAL AND MORE FAVOURABLE TREATMENT  
RECIPROCITY AND FULLER PARTICIPATION  
OF DEVELOPING COUNTRIES

*Decision of 28 November 1979  
(L/4903)*

Following negotiations within the framework of the Multilateral Trade Negotiations, the CONTRACTING PARTIES *decide* as follows:

1. Notwithstanding the provisions of Article I of the General Agreement, contracting parties may accord differential and more favourable treatment to developing countries<sup>1</sup>, without according such treatment to other contracting parties.
2. The provisions of paragraph 1 apply to the following:<sup>2</sup>
  - (a) Preferential tariff treatment accorded by developed contracting parties to products originating in developing countries in accordance with the Generalized System of Preferences,<sup>3</sup>

- (b) Differential and more favourable treatment with respect to the provisions of the General Agreement concerning non-tariff measures governed by the provisions of instruments multilaterally negotiated under the auspices of the GATT;
  - (c) Regional or global arrangements entered into amongst less-developed contracting parties for the mutual reduction or elimination of tariffs and, in accordance with criteria or conditions which may be prescribed by the CONTRACTING PARTIES, for the mutual reduction or elimination of non-tariff measures, on products imported from one another
  - (d) Special treatment of the least developed among the developing countries in the context of any general or specific measures in favour of developing countries.
3. Any differential and more favourable treatment provided under this clause:
- (a) shall be designed to facilitate and promote the trade of developing countries and not to raise barriers to or create undue difficulties for the trade of any other contracting parties;
  - (b) shall not constitute an impediment to the reduction or elimination of tariffs and other restrictions to trade on a most-favoured-nation basis;

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<sup>1</sup> The words "developing countries" as used in this text are to be understood to refer also to developing territories.

<sup>2</sup> It would remain open for the CONTRACTING PARTIES to consider on an *ad hoc* basis under the GATT provisions for joint action any proposals for differential and more favourable treatment not falling within the scope of this paragraph.

<sup>3</sup> As described in the Decision of the CONTRACTING PARTIES of 25 June 1971, relating to the establishment of "generalized, non-reciprocal and non discriminatory preferences beneficial to the developing countries" (BISD 18S/24).

- (c) shall in the case of such treatment accorded by developed contracting parties to developing countries be designed and, if necessary, modified, to respond positively to the development, financial and trade needs of developing countries.
4. Any contracting party taking action to introduce an arrangement pursuant to paragraphs 1, 2 and 3 above or subsequently taking action to introduce modification or withdrawal of the differential and more favourable treatment so provided shall:<sup>4</sup>
- (a) notify the CONTRACTING PARTIES and furnish them with all the information they may deem appropriate relating to such action;
  - (b) afford adequate opportunity for prompt consultations at the request of any interested contracting party with respect to any difficulty or matter that may arise. The CONTRACTING PARTIES shall, if requested to do so by such contracting party, consult with all contracting parties concerned with respect to the matter with a view to reaching solutions satisfactory to all such contracting parties.

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 needs.

6. Having regard to the special economic difficulties and the particular development, financial and trade needs of the least-developed countries, the developed countries shall exercise the utmost restraint in seeking any concessions or contributions for commitments made by them to reduce or remove tariffs and other barriers to the trade of such countries, and the least-developed countries shall not be expected to make concessions or contributions that are inconsistent with the recognition of their particular situation and problems.

7. The concessions and contributions made and the obligations assumed by developed and less-developed contracting parties under the provisions of the General Agreement should promote the basic objectives of the Agreement, including those embodied in the Preamble and in Article XXXVI. 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.

8. Particular account shall be taken of the serious difficulty of the least-developed countries in making concessions and contributions in view of their special economic situation and their development, financial and trade needs.

9. The contracting parties will collaborate in arrangements for review of the operation of these provisions, bearing in mind the need for individual and joint efforts by contracting parties to meet the development needs of developing countries and the objectives of the General Agreement.

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<sup>4</sup> Nothing in these provisions shall affect the rights of contracting parties under the General Agreement.

## **Waivers**

[http://www.wto.org/english/tratop\\_e/devel\\_e/d2legl\\_e.htm#wavers](http://www.wto.org/english/tratop_e/devel_e/d2legl_e.htm#wavers)

Going beyond legal provisions stated explicitly in WTO agreements, actions in favor of developing countries, individually or as a group, may also be taken under “**waivers**” from the main WTO rules.

These waivers are granted by the General Council according to procedures set out in Article IX:3 of [the Agreement Establishing the WTO](#). Recent examples of waivers include the EC/France Trading Arrangements with Morocco, the United States' Caribbean Basin Economic Recovery

Act (CBERA), the Canadian Tariff Treatment for Commonwealth Caribbean Countries (CARIBCAN), the United States' Andean Trade Preference Act, and the ACP-EC Partnership Agreement (currently under consideration).

The June 1999 General Council [Decision on Waiver regarding Preferential Tariff Treatment for Least-Developed Countries](#) (download in MS Word format, 2 pages, 35KB) allows developing country members to provide preferential tariff treatment to products of least developed countries.

## European Communities -- Conditions for the Granting of Tariff Preferences to Developing Countries (EC -- Tariff Preferences)

### Appellate Body Report, WT/DS246/AB/R, 7 April 2004

*Editorial Note: The footnote numbering does not correspond to the footnote numbering in the original report.*

Abi-Saab, Presiding Member, Baptista, Member, Sacerdoti, Member

[http://www.wto.org/english/tratop\\_e/dispu\\_e/cases\\_e/ds246\\_e.htm](http://www.wto.org/english/tratop_e/dispu_e/cases_e/ds246_e.htm)

(...)

### I. Introduction

1. The European Communities appeals certain issues of law and legal interpretations developed in the Panel Report, *European Communities – Conditions for the Granting of Tariff Preferences to Developing Countries* (the "Panel Report").<sup>238</sup> The Panel was established to consider a complaint by India against the European Communities regarding the conditions under which the European Communities accords tariff preferences to developing countries pursuant to Council Regulation (EC) No. 2501/2001 of 10 December 2001 "applying a scheme of generalised tariff preferences for the period from 1 January 2002 to 31 December 2004" (the "Regulation").<sup>239</sup>

2. The Regulation provides for five preferential tariff "arrangements"<sup>240</sup>, namely:

- (a) general arrangements described in Article 7 of the Regulation (the "General Arrangements");
- (b) special incentive arrangements for the protection of labour rights;
- (c) special incentive arrangements for the protection of the environment;
- (d) special arrangements for least-developed countries; and
- (e) special arrangements to combat drug production and trafficking (the "Drug Arrangements").<sup>241</sup>

3. All the countries listed in Annex I to the Regulation are eligible to receive tariff preferences under the General Arrangements<sup>242</sup>, which provide, broadly, for suspension of Common Customs Tariff duties on products listed as "non-sensitive" and for reduction of Common Customs Tariff *ad valorem* duties on products listed as "sensitive".<sup>243</sup> The General Arrangements are described in further detail in paragraphs 2.4 and 2.5 of the Panel Report. The four other arrangements in the Regulation provide tariff preferences *in addition* to those granted

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<sup>238</sup>WT/DS246/R, 1 December 2003.

<sup>239</sup>*Official Journal of the European Communities*, L Series, No. 346 (31 December 2001), p. 1 (Exhibit India-6 submitted by India to the Panel).

<sup>240</sup>Regulation, Art. 1.2.

<sup>241</sup>*Ibid.*

<sup>242</sup>Panel Report, para. 2.4.

<sup>243</sup>Regulation, Arts. 7.1-7.2.

under the General Arrangements.<sup>244</sup> However, only some of the country beneficiaries of the General Arrangements are also beneficiaries of the other arrangements. Specifically, preferences under the special incentive arrangements for the protection of labour rights and the special incentive arrangements for the protection of the environment are restricted to those countries that "are determined by the European Communities to comply with certain labour [or] environmental policy standards"<sup>245</sup>, respectively. Preferences under the special arrangements for least-developed countries are restricted to certain specified countries.<sup>246</sup> Finally, preferences under the Drug Arrangements are provided only to 12 predetermined countries, namely Bolivia, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Honduras, Nicaragua, Pakistan, Panama, Peru, and Venezuela.<sup>247</sup>

4. India is a beneficiary of the General Arrangements but not of the Drug Arrangements, or of any of the other arrangements established by the Regulation. In its request for the establishment of a panel, India challenged the Drug Arrangements as well as the special incentive arrangements for the protection of labour rights and the environment.<sup>248</sup> However, in a subsequent meeting with the Director-General regarding the composition of the Panel—and later in writing to the European Communities—India indicated its decision to limit its complaint to the Drug Arrangements, while reserving its right to bring additional complaints regarding the two "special incentive arrangements".<sup>249</sup> Accordingly, this dispute concerns only the Drug Arrangements.

5. The Panel summarized the effect of the Drug Arrangements as follows:

The result of the Regulation is that the tariff reductions accorded under the Drug Arrangements to the 12 beneficiary countries are greater than the tariff reductions granted under the General Arrangements to other developing countries. In respect of products that are included in the Drug Arrangements but not in the General Arrangements, the 12 beneficiary countries are granted *duty free* access to the European Communities' market, while all other developing countries must pay the *full duties applicable under the Common Customs Tariff*. In respect of products that are included in both the Drug Arrangements and the General Arrangements and that are deemed "sensitive" under column G of Annex IV to the Regulation with the exception for products of CN codes 0306 13, 1704 10 91 and 1704 10 99, the 12 beneficiary countries are granted *duty-free* access to the European Communities' market, while all other developing countries are entitled only to *reductions in the duties applicable under the Common Customs Tariff*.<sup>250</sup> (original italics)

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<sup>244</sup>*Ibid.*, Arts. 8-10. For example, these tariff preferences include further reductions in the duties imposed on certain "sensitive" products.

<sup>245</sup>Panel Report, para. 2.3. See Regulation, Arts. 14 and 21, and Annex I (Columns E and G).

<sup>246</sup>Regulation, Annex I (Column H).

<sup>247</sup>*Ibid.* (Column I); Panel Report, paras. 2.3 and 2.7.

<sup>248</sup>Request for the establishment of a panel by India, WT/DS246/4, 9 December 2002, p. 2.

<sup>249</sup>Panel Report, para. 1.5.

<sup>250</sup>*Ibid.*, para. 2.8. See also, *ibid.*, para. 2.7.

6. India requested the Panel to find that "the Drug Arrangements set out in Article 10"<sup>251</sup> of the Regulation are inconsistent with Article I:1 of the *General Agreement on Tariffs and Trade 1994* (the "GATT 1994") and are not justified by the Decision on Differential and More Favourable Treatment, Reciprocity, and Fuller Participation of Developing Countries (the "Enabling Clause").<sup>252</sup> In the Panel Report, circulated to Members of the World Trade Organization (the "WTO") on 1 December 2003, the Panel concluded that:

- (a) India has the burden of demonstrating that the European Communities' Drug Arrangements are inconsistent with Article I:1 of GATT 1994;
- (b) India has demonstrated that the European Communities' Drug Arrangements are inconsistent with Article I:1 of GATT 1994;
- (c) the European Communities has the burden of demonstrating that the Drug Arrangements are justified under paragraph 2(a) of the Enabling Clause; [and]
- (d) the European Communities has failed to demonstrate that the Drug Arrangements are justified under paragraph 2(a) of the Enabling Clause[.]<sup>253</sup>

The Panel also concluded that the European Communities had "failed to demonstrate that the Drug Arrangements are justified under Article XX(b) of GATT 1994".<sup>254</sup> Finally, the Panel concluded, pursuant to Article 3.8 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU"), that "because the Drug Arrangements are inconsistent with Article I:1 of GATT 1994 and not justified by Article 2(a) of the Enabling Clause or Article XX(b) of GATT 1994, the European Communities has nullified or impaired benefits accruing to India under GATT 1994."<sup>255</sup>

(...)

### III. Issues Raised in This Appeal

78. The following issues are raised in this appeal:

- (a) Whether the Panel erred in concluding that the "special arrangements to combat drug production and trafficking" (the "Drug Arrangements"), which are part of Council Regulation (EC) No. 2501/2001 (the "Regulation")<sup>256</sup>, are inconsistent

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<sup>251</sup>*Ibid.*, para. 3.1 (referring to India's first written submission to the Panel, para. 67).

<sup>252</sup>GATT Document L/4903, 28 November 1979, BISD 26S/203 (attached as Annex 2 to this Report).

<sup>253</sup>Panel Report, para. 8.1(a)-(d).

<sup>254</sup>*Ibid.*, para. 8.1(e).

<sup>255</sup>*Ibid.*, para. 8.1(f).

<sup>256</sup>Council Regulation (EC) No. 2501/2001 of 10 December 2001 applying a scheme of generalised tariff preferences for the period from 1 January 2002 to 31 December 2004, *Official Journal of the European Communities*, L Series, No. 346 (31 December 2001), p. 1 (Exhibit India-6 submitted by India to the Panel).

with Article I:1 of the *General Agreement on Tariffs and Trade 1994* (the "GATT 1994")<sup>257</sup>, based on the Panel's findings that:

- (i) the Decision on Differential and More Favourable Treatment, Reciprocity, and Fuller Participation of Developing Countries (the "Enabling Clause")<sup>258</sup> is an "exception"<sup>259</sup> to Article I:1 of the GATT 1994;
  - (ii) the Enabling Clause "does not exclude the applicability"<sup>260</sup> of Article I:1 of the GATT 1994; and
  - (iii) the European Communities bears the burden of invoking the Enabling Clause and proving that the Drug Arrangements are consistent with that Clause<sup>261</sup>; and
- (b) Whether the Panel erred in concluding that the European Communities failed to prove that the Drug Arrangements are justified under paragraph 2(a) of the Enabling Clause<sup>262</sup>, based on the Panel's findings that:
- (i) the term "non-discriminatory" in footnote 3 to paragraph 2(a) of the Enabling Clause requires that, pursuant to schemes under the Generalized System of Preferences ("GSP"), "identical tariff preferences"<sup>263</sup> be provided to all developing countries without differentiation, except as regards the implementation of *a priori* limitations; and
  - (ii) the term "developing countries" in paragraph 2(a) of the Enabling Clause means "all"<sup>264</sup> developing countries, except as regards the implementation of *a priori* limitations.

#### **IV. The Relationship Between Article I:1 of the GATT 1994 and the Enabling Clause**

79. We begin our analysis of the European Communities' appeal by examining its claim that the Panel improperly characterized the relationship between Article I:1 of the GATT 1994 and the Enabling Clause, and thus improperly allocated the burden of proof in this dispute.

(...)

##### **B. *Relevance of the Relationship Between Article I:1 of the GATT 1994 and the Enabling Clause for the Allocation of the Burden of Proof***

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<sup>257</sup>Panel Report, paras. 7.60 and 8.1(b).

<sup>258</sup>GATT Document L/4903, 28 November 1979, BISD 26S/203 (attached as Annex 2 to this Report).

<sup>259</sup>Panel Report, para. 7.53.

<sup>260</sup>*Ibid.*

<sup>261</sup>*Ibid.*

<sup>262</sup>*Ibid.*, para. 8.1(d).

<sup>263</sup>Panel Report, para. 7.161.

<sup>264</sup>*Ibid.*, para. 7.176.

87. We begin our analysis of the relationship between Article I:1 of the GATT 1994 and the Enabling Clause, and the attendant implications for the allocation of the burden of proof in this dispute, by recalling the observation of the Appellate Body in *US – Wool Shirts and Blouses*:

[I]t is a generally-accepted canon of evidence in civil law, common law and, in fact, most jurisdictions, that the burden of proof rests upon the party, whether complaining or defending, who asserts the affirmative of a particular claim or defence.<sup>265</sup>

It is thus for the *complaining* party to raise a claim with respect to a particular obligation and to *prove* that the responding party is acting inconsistently with that obligation. It is for the *responding* party, if it so chooses, to raise a defence in response to an allegation of inconsistency and to *prove* that its challenged measure satisfies the conditions of that defence. Therefore, the question before us is whether India must raise a "claim" and prove that the Drug Arrangements are inconsistent with the Enabling Clause, or whether the European Communities must raise and prove, in "defence", that the Drug Arrangements are consistent with the Enabling Clause, in order to justify the alleged inconsistency of the Drug Arrangements with Article I:1.<sup>266</sup>

88. We recall that the Appellate Body has addressed the allocation of the burden of proof in similar situations. In cases where one provision permits, in certain circumstances, behaviour that would otherwise be inconsistent with an obligation in another provision, and one of the two provisions refers to the other provision, the Appellate Body has found that the complaining party bears the burden of establishing that a challenged measure is inconsistent with the provision permitting particular behaviour *only* where one of the provisions suggests that the obligation is not applicable to the said measure.<sup>267</sup> Otherwise, the permissive provision has been characterized as an exception, or defence, and the onus of invoking it and proving the consistency of the measure with its requirements has been placed on the responding party.<sup>268</sup> However, this distinction may not always be evident or readily applicable.

### C. *Characterization of the Enabling Clause*

#### 1. Text of Article I:1 and the Enabling Clause

89. In considering whether the Enabling Clause is an exception to Article I:1 of the GATT 1994, we look, first, to the text of the provisions at issue. Article I:1, which embodies the MFN principle, provides:

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<sup>265</sup>Appellate Body Report, *US – Wool Shirts and Blouses*, p. 14, DSR 1997:I, at 335.

<sup>266</sup>We are not concerned here with the situation where a complaining party brings a challenge solely under the provisions of the Enabling Clause, that is, without also claiming an inconsistency with Article I of the GATT 1994.

<sup>267</sup>See Appellate Body Report, *EC – Hormones*, para. 104; Appellate Body Report, *Brazil – Aircraft*, paras. 139-141; and Appellate Body Report, *EC – Sardines*, para. 275.

<sup>268</sup>See Appellate Body Report, *US – FSC (Article 21.5 – EC)*, paras. 131-133; and Appellate Body Report, *US – Wool Shirts and Blouses*, p.16, DSR 1997:I, at 337.

## Article I

### General Most-Favoured-Nation Treatment

1. With respect to customs duties and charges of any kind imposed on or in connection with importation or exportation or imposed on the international transfer of payments for imports or exports, and with respect to the method of levying such duties and charges, and with respect to all rules and formalities in connection with importation and exportation, and with respect to all matters referred to in paragraphs 2 and 4 of Article III,\* any advantage, favour, privilege or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other contracting parties.

Article I:1 plainly imposes upon WTO Members the obligation to treat "like products ... equally, irrespective of their origin".<sup>269</sup>

90. We turn now to the Enabling Clause, which has become an integral part of the GATT 1994.<sup>270</sup> Paragraph 1 of the Enabling Clause, which applies to all measures authorized by that Clause, provides:

Notwithstanding the provisions of Article I of the General Agreement, contracting parties may accord differential and more favourable treatment to developing countries, without according such treatment to other contracting parties. (footnote omitted)

The ordinary meaning of the term "notwithstanding" is, as the Panel noted<sup>271</sup>, "[i]n spite of, without regard to or prevention by".<sup>272</sup> By using the word "notwithstanding", paragraph 1 of the Enabling Clause permits Members to provide "differential and more favourable treatment" to developing countries "in spite of" the MFN obligation of Article I:1. Such treatment would otherwise be inconsistent with Article I:1 because that treatment is not extended to all Members of the WTO

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<sup>269</sup> Appellate Body Report, *EC – Bananas III*, para. 190.

<sup>270</sup> In response to questioning at the oral hearing, the participants and third participants agreed that the Enabling Clause is one of the "other decisions of the CONTRACTING PARTIES" within the meaning of paragraph 1(b)(iv) of the language of Annex 1A incorporating the GATT 1994 into the *WTO Agreement*. That provision stipulates that:

1. The General Agreement on Tariffs and Trade 1994 ("GATT 1994") shall consist of:
  - ...
  - (b) the provisions of the legal instruments set forth below that have entered into force under the GATT 1947 before the date of entry into force of the WTO Agreement:
    - ...
    - (iv) other decisions of the CONTRACTING PARTIES to GATT 1947[.]

<sup>271</sup> See Panel Report, para. 7.44.

<sup>272</sup> *Shorter Oxford English Dictionary*, 5th ed., W.R. Trumble, A. Stevenson (eds.) (Oxford University Press, 2002), Vol. 2, p. 1948.

"immediately and unconditionally".<sup>273</sup> Paragraph 1 thus excepts Members from complying with the obligation contained in Article I:1 for the purpose of providing differential and more favourable treatment to developing countries, provided that such treatment is in accordance with the conditions set out in the Enabling Clause. As such, the Enabling Clause operates as an "exception" to Article I:1.

## 2. Object and Purpose of the *WTO Agreement* and the Enabling Clause

91. The European Communities' contention that the Enabling Clause is *not* in the nature of an exception appears to be founded on the European Communities' understanding of the object and purpose of the *Marrakesh Agreement Establishing the World Trade Organization* (the "*WTO Agreement*") and the Enabling Clause. We, too, look to the object and purpose of the *WTO Agreement* and the Enabling Clause to clarify whether the Enabling Clause was intended to operate as an exception to Article I:1.

92. The Preamble to the *WTO Agreement* provides that Members recognize:

... that there is need for *positive efforts* designed to ensure that developing countries, and especially the least developed among them, secure a share in the growth in international trade commensurate with the needs of their economic development[.]<sup>274</sup> (emphasis added)

The Waiver Decision on the Generalized System of Preferences (the "1971 Waiver Decision")<sup>275</sup>, which provided the initial authorization under the GATT for developed countries' GSP schemes and is explicitly referred to in footnote 3 of the Enabling Clause<sup>276</sup>, offers relevant guidance in discerning the object and purpose of the Enabling Clause. In the Preamble to the 1971 Waiver Decision, the Contracting Parties recognized:

... that a principal aim of the CONTRACTING PARTIES is promotion of the trade and export earnings of developing countries for the furtherance of their economic development;

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<sup>273</sup>GATT 1994, Art. I:1.

<sup>274</sup>Second recital. We note that Article XXXVI:3 of the GATT 1994 similarly provides:  
There is need for positive efforts designed to ensure that less-developed contracting parties secure a share in the growth in international trade commensurate with the needs of their economic development.

<sup>275</sup>GATT Document L/3545, 25 June 1971, BISD 18S/24 (attached as Annex D-2 to the Panel Report).

<sup>276</sup>Footnote 3 of the Enabling Clause states:

As described in the Decision of the CONTRACTING PARTIES of 25 June 1971, relating to the establishment of "generalized, non-reciprocal and non discriminatory preferences beneficial to the developing countries" (BISD 18S/24).

[and recognized] further that individual and joint action is essential to further the development of the economies of developing countries[.]<sup>277</sup>

We understand, therefore, that the Enabling Clause is among the "positive efforts" called for in the Preamble to the *WTO Agreement* to be taken by developed-country Members to enhance the "economic development" of developing-country Members.<sup>278</sup>

93. According to the European Communities, the Enabling Clause, as the "most concrete, comprehensive and important application of the principle of Special and Differential Treatment", serves "to achieve one of the fundamental objectives of the *WTO Agreement*".<sup>279</sup> In the view of the European Communities, provisions that are exceptions permit Members to adopt measures to pursue objectives that are "not ... among the *WTO Agreement*'s own objectives"<sup>280</sup>; the Enabling Clause thus does not fall under the category of exceptions. Pointing to this alleged difference between the role of measures falling under the Enabling Clause and that of measures falling under exception provisions such as Article XX, the European Communities contends that the *WTO Agreement* does not "merely tolerate" measures under the Enabling Clause, but rather "encourages" developed-country Members to adopt such measures.<sup>281</sup> According to the European Communities, to require preference-granting countries to invoke the Enabling Clause in order to justify or defend their GSP schemes cannot be reconciled with the intention of *WTO* Members to encourage these schemes.

94. We note, however, as did the Panel<sup>282</sup>, that *WTO* objectives may well be pursued through measures taken under provisions characterized as exceptions. The Preamble to the *WTO Agreement* identifies certain objectives that may be pursued by Members through measures that would have to be justified under the "General Exceptions" of Article XX. For instance, one such objective is reflected in the recognition by Members that the expansion of trade must be accompanied by:

... the optimal use of the world's resources in accordance with the objective of sustainable development, [with Members] seeking both to protect and preserve the environment and to enhance the means for doing so in a manner consistent with their respective needs and concerns at different levels of economic development[.]<sup>283</sup>

95. As the Appellate Body observed in *US – Shrimp*, *WTO* Members retained Article XX(g) from the *General Agreement on Tariffs and Trade 1947* (the "GATT 1947")

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<sup>277</sup>First and second recitals. Similarly, Article XXXVI:1(d) of the GATT 1994 provides:

[I]ndividual and joint action is essential to further the development of the economies of less-developed contracting parties and to bring about a rapid advance in the standards of living in these countries[.]

<sup>278</sup>We discuss further the role of the Enabling Clause in the context of the covered agreements, *infra*, paras. **Error! Reference source not found.-Error! Reference source not found.**

<sup>279</sup>European Communities' appellant's submission, para. 20.

<sup>280</sup>*Ibid.*, para. 52.

<sup>281</sup>*Ibid.*, para. 53.

<sup>282</sup>See Panel Report, para. 7.52.

<sup>283</sup>*WTO Agreement*, Preamble, first recital.

without alteration after the conclusion of the Uruguay Round, being "fully aware of the importance and legitimacy of environmental protection as a goal of national and international policy".<sup>284</sup> Article XX(g) of the GATT 1994 permits Members, subject to certain conditions, to take measures "relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption". It is well-established that Article XX(g) is an *exception* in relation to which the responding party bears the burden of proof.<sup>285</sup> Thus, by authorizing in Article XX(g) measures for environmental conservation, an important objective referred to in the Preamble to the *WTO Agreement*, Members implicitly recognized that the implementation of such measures would not be discouraged simply because Article XX(g) constitutes a defence to otherwise WTO-inconsistent measures. Likewise, characterizing the Enabling Clause as an exception, in our view, does not undermine the importance of the Enabling Clause within the overall framework of the covered agreements and as a "positive effort" to enhance economic development of developing-country Members. Nor does it "discourag[e]"<sup>286</sup> developed countries from adopting measures in favour of developing countries under the Enabling Clause.

96. The European Communities acknowledges that requiring Members to pursue environmental measures through Article XX(g), an exception provision, may be logical because "the WTO Agreement is not an environmental agreement and ... it contains no positive regulation of environmental matters."<sup>287</sup> Because the *WTO Agreement* "regulate[s] positively the use of trade measures"<sup>288</sup>, however, and the Enabling Clause "promotes" the use of trade measures to further the development of developing countries, the European Communities argues that Members should not be required to prove the consistency of their measures with the Enabling Clause.

97. We do not consider it relevant, for the purposes of determining whether a provision is or is not in the nature of an exception, that the provision governs "trade measures" rather than measures of a primarily "non-trade" nature. Indeed, in a previous appeal, the Appellate Body found that the proviso to Article XVIII:11 of the GATT 1994—a provision authorizing quantitative restrictions when taken in response to balance-of-payments difficulties—is a defence to be invoked by the responding party.<sup>289</sup> The fact that a provision regulates the use of "trade measures", therefore, does not compel a finding that it is for the complaining party to establish inconsistency with that provision, rather than for the defending party to rely on it as a defence.

98. In sum, in our view, 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 favourable treatment". The status and relative importance of a given provision does not depend on whether it is characterized, for the purpose of allocating the burden of proof, as a claim to be proven by the

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<sup>284</sup> Appellate Body Report, *US – Shrimp*, para. 129.

<sup>285</sup> *Ibid.*, para. 157; Appellate Body Report, *US – Wool Shirts and Blouses*, pp. 15-16, DSR 1997:I, at 337 (referring to GATT Panel Report, *Canada – FIRA*, para. 5.20; GATT Panel Report, *US – Section 337*, para. 5.27; GATT Panel Report, *US – Malt Beverages*, paras. 5.43 and 5.52; and Panel Report, *US – Gasoline*, para. 6.20).

<sup>286</sup> United States' third participant's submission, para. 9.

<sup>287</sup> European Communities' appellant's submission, para. 54.

<sup>288</sup> European Communities' appellant's submission, para. 54.

<sup>289</sup> Appellate Body Report, *India – Quantitative Restrictions*, paras. 134-136. We also note that GATT panels determined Article XI:2(c) of the GATT 1947 to constitute an "exception", even though that provision addresses "trade measures", namely quantitative restrictions. (See GATT Panel Report, *Japan – Agricultural Products I*, para. 5.1.3.7; GATT Panel Report, *EEC – Dessert Apples*, para. 12.3; and GATT Panel Report, *Canada – Ice Cream and Yoghurt*, para. 59)

complaining party, or as a defence to be established by the responding party. Whatever its characterization, a provision of the covered agreements must be interpreted in accordance with the "customary rules of interpretation of public international law", as required by Article 3.2 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU").<sup>290</sup> Members' rights under the Enabling Clause are not curtailed by requiring preference-granting countries to establish in dispute settlement the consistency of their preferential measures with the conditions of the Enabling Clause. Nor does characterizing the Enabling Clause as an exception detract from its critical role in encouraging the granting of special and differential treatment to developing-country Members of the WTO.

99. In the light of the above, we *uphold* the Panel's finding, in paragraph 7.53 of the Panel Report, that the Enabling Clause is an "exception" to Article I:1 of the GATT 1994.

(...)

## V. Whether the Drug Arrangements are Justified Under the Enabling Clause

126. The European Communities "appeals subsidiarily" the Panel's finding that the Drug Arrangements are not justified under paragraph 2(a), should we "conclude that the Enabling Clause is an exception to GATT Article I:1, or that India made a valid claim under the Enabling Clause".<sup>291</sup> Having found that the Enabling Clause is in the nature of an exception to Article I:1 of the GATT 1994, we proceed to examine the European Communities' appeal as it relates to paragraph 2(a) of the Enabling Clause.

127. The European Communities challenges three of the Panel's findings, namely that:

- (a) "the term 'non-discriminatory' in footnote 3 [to paragraph 2(a) of the Enabling Clause] requires that identical tariff preferences under GSP schemes be provided to all developing countries without differentiation, except for the implementation of a priori limitations"<sup>292</sup>;
- (b) "the term 'developing countries' in paragraph 2(a) [of the Enabling Clause] should be interpreted to mean *all* developing countries, with the exception that where developed countries are implementing a priori limitations, 'developing countries' may mean *less than all* developing countries"<sup>293</sup>; and, ultimately, that

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<sup>290</sup>In this regard, we recall the Appellate Body's statement in *EC – Hormones* that:

... merely characterizing a treaty provision as an "exception" does not by itself justify a "stricter" or "narrower" interpretation of that provision than would be warranted by examination of the ordinary meaning of the actual treaty words, viewed in context and in the light of the treaty's object and purpose, or, in other words, by applying the normal rules of treaty interpretation.

(Appellate Body Report, para. 104)

<sup>291</sup>European Communities' appellant's submission, para. 67.

<sup>292</sup>Panel Report, paras. 7.161 and 7.176.

<sup>293</sup>*Ibid.*, para. 7.174. (original italics; footnote omitted)

- (c) the European Communities failed "to demonstrate that the Drug Arrangements are justified under paragraph 2(a) of the Enabling Clause".<sup>294</sup>

(...)

B. *Interpretation of the Term "Non-Discriminatory" in Footnote 3 to Paragraph 2(a) of the Enabling Clause*

142. We proceed to interpret the term "non-discriminatory" as it appears in footnote 3 to paragraph 2(a) of the Enabling Clause.

143. We recall first that the Enabling Clause has become a part of the GATT 1994.<sup>295</sup> Paragraph 1 of the Enabling Clause authorizes WTO Members to provide "differential and more favourable treatment to developing countries, without according such treatment to other WTO Members". As explained above, such differential treatment is permitted "notwithstanding" the provisions of Article I of the GATT 1994. Paragraph 2(a) and footnote 3 thereto clarify that paragraph 1 applies to "[p]referential tariff treatment accorded by developed contracting parties to products originating in developing countries in accordance with the Generalized System of Preferences"<sup>296</sup>, "[a]s described in the [1971 Waiver Decision], relating to the establishment of 'generalized, non-reciprocal and non discriminatory preferences beneficial to the developing countries'".<sup>297</sup>

144. The Preamble to the 1971 Waiver Decision in turn refers to "preferential tariff treatment" in the following terms:

*Recalling* that at the Second UNCTAD, unanimous agreement was reached in favour of the early establishment of a mutually acceptable system of generalized, non-reciprocal and non-discriminatory preferences beneficial to the developing countries in order to increase the export earnings, to promote the industrialization, and to accelerate the rates of economic growth of these countries;

*Considering* that mutually acceptable arrangements have been drawn up in the UNCTAD concerning the establishment of generalized, non-discriminatory, non-reciprocal preferential tariff treatment in the markets of developed countries for products originating in developing countries[.]<sup>298</sup> (original italics; underlining added)

145. Paragraph 2(a) of the Enabling Clause provides, therefore, that, to be justified under that provision, preferential tariff treatment must be "in accordance" with the GSP "as described" in the *Preamble* to the 1971 Waiver Decision. "Accordance" being defined in the dictionary as

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<sup>294</sup>*Ibid.*, para. 8.1(d).

<sup>295</sup>See *supra*, footnote **Error! Bookmark not defined.**

<sup>296</sup>Enabling Clause, para. 2(a) (attached as Annex 2 to this Report).

<sup>297</sup>*Ibid.*, footnote 3 to para. 2(a).

<sup>298</sup>1971 Waiver Decision, third and fourth recitals.

"conformity"<sup>299</sup>, only preferential tariff treatment that is in conformity with the description "generalized, non-reciprocal and non-discriminatory" treatment can be justified under paragraph 2(a).

146. In the light of the above, we do not agree with European Communities' assertion<sup>300</sup> that the Panel's interpretation of the word "non-discriminatory" in footnote 3 of the Enabling Clause is erroneous because the phrase "generalized, non-reciprocal and non discriminatory" in footnote 3 merely refers to the description of the GSP in the 1971 Waiver Decision and, of itself, does not impose any legal obligation on preference-granting countries. Nor do we agree with the United States that the Panel erred in "assum[ing]" that the term "non-discriminatory" in footnote 3 imposes obligations on preference-granting countries, and that, instead, footnote 3 "is simply a cross-reference to where the Generalized System of Preferences is described."<sup>301</sup>

147. We find support for our interpretation in the French version of paragraph 2(a) of the Enabling Clause, requiring that the tariff preferences be accorded "*conformément au Système généralisé de préférences*". The term "in accordance" is thus "*conformément*" in the French version. In addition, the phrase "[a]s described in [the 1971 Waiver Decision]" in footnote 3 is stated as "[t]el qu'il est défini dans la décision des PARTIES CONTRACTANTES en date du 25 juin 1971". Similarly, the Spanish version uses the terms "*conformidad*" and "[t]al como lo define la Decisión de las PARTES CONTRATANTES de 25 de junio de 1971". In our view, the stronger, more obligatory language in both the French and Spanish texts—that is, using "as defined in" rather than "as described in"—lends support to our view that only preferential tariff treatment that is "generalized, non-reciprocal and non-discriminatory" is covered under paragraph 2(a) of the Enabling Clause.<sup>302</sup>

148. Having found that the qualification of the GSP as "generalized, non-reciprocal and non discriminatory" imposes obligations that must be fulfilled for preferential tariff treatment to be justified under paragraph 2(a), we turn to address the Panel's finding that:

... the term "non-discriminatory" in footnote 3 requires that *identical* tariff preferences under GSP schemes be provided to *all* developing countries without differentiation, except for the implementation of a priori limitations.<sup>303</sup> (emphasis added)

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<sup>299</sup>*Shorter Oxford English Dictionary*, 5th ed., W.R. Trumble, A. Stevenson (eds.) (Oxford University Press, 2002), Vol. 1, p. 15.

<sup>300</sup>European Communities' response to questioning at the oral hearing.

<sup>301</sup>United States' third participant's submission, para. 11.

<sup>302</sup>We further note the existence of a 1999 WTO waiver allowing *developing* countries to grant special preferences to *least-developed* countries. (Waiver Decision on Preferential Tariff Treatment for Least-Developed Countries, WT/L/304, 15 June 1999 (the "1999 LDC Waiver")) That waiver applies only to "preferential tariff treatment ... provided on a generalized, non-reciprocal and non-discriminatory basis". (*Ibid.*, para. 2) As such, for tariff preferences to be justified thereunder, there is a *requirement* that the treatment be accorded on a "generalized, non-reciprocal and non-discriminatory *basis*." (emphasis added) We see no reason why *developed* countries would be permitted to provide preferential tariff treatment to developing countries under the Enabling Clause other than on a "non-discriminatory basis", when there is clearly a requirement for *developing* countries to provide such treatment to least-developed countries on a "non-discriminatory basis" under the 1999 LDC Waiver.

<sup>303</sup>Panel Report, para. 7.161.

149. The European Communities maintains that "'non-discrimination' is not synonymous with formally equal treatment"<sup>304</sup> and that "[t]reating differently situations which are objectively different is not discriminatory."<sup>305</sup> The European Communities asserts that "[t]he objective of the Enabling Clause is different from that of Article I:1 of the GATT."<sup>306</sup> In its view, the latter is concerned with "providing equal conditions of competition for imports of like products originating in all Members", whereas "the Enabling Clause is a form of Special and Differential Treatment for developing countries, which seeks the opposite result: to create unequal competitive opportunities in order to respond to the special needs of developing countries."<sup>307</sup> The European Communities derives contextual support from paragraph 3(c), which states that the treatment provided under the Enabling Clause "shall ... be designed and, if necessary, modified, to respond positively to the development, financial and trade needs of developing countries." The European Communities concludes that the term "non-discriminatory" in footnote 3 "does not prevent the preference-giving countries from differentiating between developing countries which have different development needs, where tariff differentiation constitutes an adequate response to such differences."<sup>308</sup>

150. India, in contrast, asserts that "non-discrimination in respect of tariff measures refers to formally equal[] treatment"<sup>309</sup> and that paragraph 2(a) of the Enabling Clause requires that "preferential tariff treatment [be] applied equally" among developing countries.<sup>310</sup> In support of its argument, India submits that an interpretation of paragraph 2(a) of the Enabling Clause that authorizes developed countries to provide "discriminatory tariff treatment *in favour of the developing countries* but not *between the developing countries* gives full effect to both Article I of the GATT and paragraph 2(a) of the Enabling Clause and minimises the conflict between them."<sup>311</sup> India emphasizes that, by consenting to the adoption of the Enabling Clause, developing countries did not "relinquish[] their MFN rights [under Article I of the GATT 1994] as between themselves, thus permitting developed countries to discriminate between them."<sup>312</sup>

151. We examine now the ordinary meaning of the term "non-discriminatory" in footnote 3 to paragraph 2(a) of the Enabling Clause. As we observed, footnote 3 requires that GSP schemes under the Enabling Clause be "generalized, non-reciprocal and non discriminatory". Before the Panel, the participants offered competing definitions of the word "discriminate". India suggested that this word means "'to make or constitute a difference in or between; distinguish' and 'to make a distinction in the treatment of different categories of peoples or things'."<sup>313</sup> The European Communities, however, understood this word to mean "'to make a distinction in the treatment of different categories of people or things, esp. *unjustly* or *prejudicially* against people on grounds of race, colour, sex, social status, age, etc.'"<sup>314</sup>

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<sup>304</sup>European Communities' appellant's submission, para. 71.

<sup>305</sup>*Ibid.*

<sup>306</sup>*Ibid.*, para. 152.

<sup>307</sup>*Ibid.*

<sup>308</sup>*Ibid.*, para. 188.

<sup>309</sup>India's appellee's submission, para. 120.

<sup>310</sup>*Ibid.*, para. 106.

<sup>311</sup>*Ibid.*, para. 92. (original italics)

<sup>312</sup>India's appellee's submission, para. 104.

<sup>313</sup>Panel Report, para. 7.126 (quoting *The New Shorter Oxford English Dictionary*, L. Brown (ed.) (Clarendon Press, 1993), Vol. 1, p. 689).

<sup>314</sup>*Ibid.* (quoting *The New Shorter Oxford English Dictionary*, L. Brown (ed.) (Clarendon Press, 1993), Vol. 1, p. 689). (italics added by the Panel)

152. Both definitions can be considered as reflecting ordinary meanings of the term "discriminate"<sup>315</sup> and essentially exhaust the relevant ordinary meanings. The principal distinction between these definitions, as the Panel noted, is that India's conveys a "*neutral* meaning of making a distinction", whereas the European Communities' conveys a "*negative* meaning carrying the connotation of a distinction that is unjust or prejudicial."<sup>316</sup> Accordingly, the ordinary meanings of "discriminate" point in conflicting directions with respect to the propriety of according differential treatment. Under India's reading, any differential treatment of GSP beneficiaries would be prohibited, because such treatment necessarily makes a distinction between beneficiaries. In contrast, under the European Communities' reading, differential treatment of GSP beneficiaries would not be prohibited *per se*. Rather, distinctions would be impermissible only where the basis for such distinctions was improper. Given these divergent meanings, we do not regard the term "non-discriminatory", on its own, as determinative of the permissibility of a preference-granting country according different tariff preferences to different beneficiaries of its GSP scheme.

153. Nevertheless, at this stage of our analysis, we are able to discern some of the content of the "non-discrimination" obligation based on the ordinary meanings of that term. Whether the drawing of distinctions is *per se* discriminatory, or whether it is discriminatory only if done on an improper basis, the ordinary meanings of "discriminate" converge in one important respect: they both suggest that distinguishing among similarly-situated beneficiaries is discriminatory. For example, India suggests that all beneficiaries of a particular Member's GSP scheme are similarly-situated, implicitly arguing that any differential treatment of such beneficiaries constitutes discrimination. The European Communities, however, appears to regard GSP beneficiaries as similarly-situated when they have "similar development needs".<sup>317</sup> Although the European Communities acknowledges that differentiating between similarly-situated GSP beneficiaries would be inconsistent with footnote 3 of the Enabling Clause, it submits that there is no inconsistency in differentiating between GSP beneficiaries with "different development needs".<sup>318</sup> Thus, based on the ordinary meanings of "discriminate", India and the European Communities effectively appear to agree that, pursuant to the term "non-discriminatory" in footnote 3, similarly-situated GSP beneficiaries should not be treated differently.<sup>319</sup> The

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<sup>315</sup>See *Shorter Oxford English Dictionary*, 5th ed., W.R. Trumble, A. Stevenson (eds.) (Oxford University Press, 2002), Vol. 1, p. 697.

<sup>316</sup>Panel Report, para. 7.126. (original italics)

<sup>317</sup>European Communities' appellant's submission, para. 175. (See also, *ibid.*, para. 186)

<sup>318</sup>*Ibid.*, para. 188.

<sup>319</sup>We note that the contrasting definitions proffered by the participants, as well as the convergence of those definitions on the fact that similarly-situated entities should not be treated differently, find reflection in the use of the term "discrimination" in general international law. In this respect, we note, as an example, the definitions of "discrimination" provided by the European Communities, in footnotes 56 and 57 of its appellant's submission:

<sup>56</sup>... Mere differences of treatment do not necessarily constitute discrimination ... discrimination may in general be said to arise where those who are in all material respects the same are treated differently, or where those who are in material respects different are treated in the same way.

(quoting R. Jennings and A. Watts (eds.), *Oppenheim's International Law*, 9th ed. (Longman, 1992), Vol. I, p. 378)

<sup>57</sup>... Discrimination occurs when in a legal system an inequality is introduced in the enjoyment of a certain right, or in a duty, while there is no sufficient connection between the inequality upon which the legal

participants disagree only as to the basis for determining whether beneficiaries are similarly-situated.

154. Paragraph 2(a), on its face, does not explicitly authorize or prohibit the granting of different tariff preferences to different GSP beneficiaries. It is clear from the ordinary meanings of "non-discriminatory", however, that preference-granting countries must make available identical tariff preferences to all similarly-situated beneficiaries.

155. We continue our interpretive analysis by turning to the immediate context of the term "non-discriminatory". We note first that footnote 3 to paragraph 2(a) stipulates that, in addition to being "non-discriminatory", tariff preferences provided under GSP schemes must be "generalized". According to the ordinary meaning of that term, tariff preferences provided under GSP schemes must be "generalized" in the sense that they "apply more generally; [or] become extended in application".<sup>320</sup> However, this ordinary meaning alone may not reflect the entire significance of the word "generalized" in the context of footnote 3 of the Enabling Clause, particularly because that word resulted from lengthy negotiations leading to the GSP. In this regard, we note the Panel's finding that, by requiring tariff preferences under the GSP to be "generalized", developed and developing countries together sought to eliminate existing "special" preferences that were granted only to certain designated developing countries.<sup>321</sup> Similarly, in response to our questioning at the oral hearing, the participants agreed that one of the objectives of the 1971 Waiver Decision and the Enabling Clause was to eliminate the fragmented system of special preferences<sup>322</sup> that were, in general, based on historical and political ties between developed countries and their former colonies.

156. 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. In concluding otherwise, the Panel assumed that allowing tariff preferences such as the Drug Arrangements would necessarily "result [in] the collapse of the whole GSP system and a return back to special preferences favouring selected developing countries".<sup>323</sup> To us, this conclusion is unwarranted. We observe that the term "generalized" requires that the GSP schemes of preference-granting countries remain generally applicable.<sup>324</sup>

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inequality is based, and the right or the duty in which this inequality is made.

(quoting E.W. Vierdag, *The Concept of Discrimination in International Law*, (Martinus Nijhoff, 1973), p. 61)

<sup>320</sup>*Shorter Oxford English Dictionary*, 5th ed., W.R. Trumble, A. Stevenson (eds.) (Oxford University Press, 2002), Vol. 1, p. 1082.

<sup>321</sup>Panel Report, paras. 7.135-7.137. The Panel also observed that statements by developed and developing countries indicated the aim of providing GSP schemes with a broad scope, encompassing the granting of preferences by *all* developed countries to *all* developing countries. (*Ibid.*, paras. 7.131-7.132)

<sup>322</sup>See also European Communities' appellant's submission, para. 175.

<sup>323</sup>Panel Report, para. 7.102.

<sup>324</sup>The European Communities argues in this respect that the GATT Contracting Parties and the WTO Members have granted a number of waivers, as mentioned in the Panel Report, for tariff preferences that are "confined *ab initio* and permanently to a limited number of developing countries located in a certain geographical region". (European Communities' appellant's submission, paras. 184-185 (referring to Panel Report, para. 7.160)) See also, Panel Report, footnote 31 to para. 4.32 (referring to Waiver Decision on the Caribbean Basin Economic Recovery Act, GATT Document L/5779, 15 February 1985, BISD 31S/20, renewed 15 November 1995, WT/L/104; Waiver Decision on CARIBCAN, GATT Document L/6102, 28 November 1986, BISD 33S/97, renewed 14 October 1996, WT/L/185; Waiver Decision on the United States – Andean Trade Preference Act, GATT Document L/6991, 19 March 1992, BISD 39S/385, renewed

Moreover, unlike the Panel, we believe that the Enabling Clause sets out sufficient conditions on the granting of preferences to protect against such an outcome. As we discuss below<sup>325</sup>, provisions such as paragraphs 3(a) and 3(c) of the Enabling Clause impose specific conditions on the granting of different tariff preferences among GSP beneficiaries.

157. As further context for the term "non-discriminatory" in footnote 3, we turn next to paragraph 3(c) of the Enabling Clause, which specifies that "differential and more favourable treatment" provided under the Enabling Clause:

... shall in the case of such treatment accorded by developed contracting parties to developing countries be designed and, if necessary, modified, to respond positively to the development, financial and trade needs of developing countries.

158. At the outset, we note that the use of the word "shall" in paragraph 3(c) suggests that paragraph 3(c) sets out an obligation for developed-country Members in providing preferential treatment under a GSP scheme to "respond positively" to the "needs of developing countries".<sup>326</sup> Having said this, we turn to consider whether the "development, financial and trade needs of developing countries" to which preference-granting countries are required to respond when granting preferences must be understood to cover the "needs" of developing countries *collectively*.

159. The Panel found that "the only appropriate way [under paragraph 3(c) of the Enabling Clause] of responding to the differing development needs of developing countries is for preference-giving countries to ensure that their [GSP] schemes have sufficient breadth of product coverage and depth of tariff cuts to respond positively to those differing needs."<sup>327</sup> In reaching this conclusion, the Panel appears to have placed a great deal of significance on the fact that paragraph 3(c) does not refer to needs of "*individual*" developing countries.<sup>328</sup> The Panel thus understood that paragraph 3(c) does not permit the granting of preferential tariff treatment exclusively to a sub-category of developing countries on the basis of needs that are common to or shared by only those developing countries. We see no basis for such a conclusion in the text of paragraph 3(c). Paragraph 3(c) refers generally to "the development, financial and trade needs of developing countries". The absence of an explicit requirement in the text of paragraph 3(c)<sup>329</sup> to respond to the needs of "all" developing countries, or to the needs of "each and every"<sup>330</sup> developing country, suggests to us that, in fact, that provision imposes no such obligation.<sup>331</sup>

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14 October 1996, WT/L/184; Waiver Decision on The Fourth ACP-EEC Convention of Lomé, GATT Document L/7604, 9 December 1994, BISD 41S/26, renewed 14 October 1996, WT/L/186; and Waiver Decision on European Communities – The ACP-EC Partnership Agreement, WT/MIN (01)/15, 14 November 2001.

<sup>325</sup>*Infra*, paras. 0-**Error! Bookmark not defined.**

<sup>326</sup>We note that the European Communities agreed before the Panel that paragraph 3(c) of the Enabling Clause sets forth a "requirement". (European Communities' first written submission to the Panel, paras. 71 and 149)

<sup>327</sup>Panel Report, para. 7.149. (See also, *ibid.*, paras. 7.95-7.97 and 7.105)

<sup>328</sup>*Ibid.*, para. 7.78.

<sup>329</sup>The United States refers to Article 3.2 of the DSU to support its argument that "panels are barred from reading legal obligations into the Enabling Clause that are not found in the text." (United States' third participant's submission, para. 13)

<sup>330</sup>Panel Report, para. 7.105. (italics omitted)

<sup>331</sup>In this respect, we agree with the European Communities that paragraph 3(c) should "be interpreted in a

160. Furthermore, as we understand it, the participants in this case agree that developing countries may have "development, financial and trade needs" that are subject to change and that certain development needs may be common to only a certain number of developing countries.<sup>332</sup> We see no reason to disagree. Indeed, paragraph 3(c) contemplates that "differential and more favourable treatment"<sup>333</sup> accorded by developed to developing countries may need to be "modified" in order to "respond positively" to the needs of developing countries. Paragraph 7 of the Enabling Clause supports this view by recording the expectation of "less-developed contracting parties" that their capacity to make contributions or concessions under the GATT will "improve with the progressive development of their economies and improvement in their trade situation". Moreover, the very purpose of the special and differential treatment permitted under the Enabling Clause is to foster economic development of developing countries. It is simply unrealistic to assume that such development will be in lockstep for all developing countries at once, now and for the future.

161. In addition, the Preamble to the *WTO Agreement*, which informs all the covered agreements including the GATT 1994 (and, hence, the Enabling Clause), explicitly recognizes the "need for positive efforts designed to ensure that developing countries, and especially the least developed among them, secure a share in the growth in international trade commensurate with the needs of their economic development".<sup>334</sup> The word "commensurate" in this phrase appears to leave open the possibility that developing countries may have different needs according to their levels of development and particular circumstances. The Preamble to the *WTO Agreement* further recognizes that Members' "respective needs and concerns at different levels of economic development"<sup>335</sup> may vary according to the different stages of development of different Members.

162. In sum, we read paragraph 3(c) as authorizing preference-granting countries to "respond positively" to "needs" that are *not* necessarily common or shared by all developing countries. Responding to the "needs of developing countries" may thus entail treating different developing-country beneficiaries differently.

163. However, paragraph 3(c) does not authorize *any* kind of response to *any* claimed need of developing countries. First, we observe that the types of needs to which a response is envisaged are limited to "development, financial and trade needs". In our view, a "need" cannot be characterized as one of the specified "needs of developing countries" in the sense of paragraph 3(c) based merely on an assertion to that effect by, for instance, a preference-granting country or a beneficiary country. Rather, when a claim of inconsistency with paragraph 3(c) is made, the existence of a "development, financial [or] trade need" must be assessed according to

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manner which, while preserving its relevance, is both workable for developed countries and consistent with the requirements that the preferences be *non-discriminatory*." (European Communities' appellant's submission, para. 138 (original italics))

<sup>332</sup>The European Communities emphasized before the Panel that the "development, financial and trade needs of developing countries" referred to in paragraph 3(c) of the Enabling Clause "[o]bviously ... may vary between different categories of developing countries, as well as over time." (European Communities' first written submission to the Panel, para. 71) That "needs of developing countries" may change over time was also acknowledged by India in response to our questioning at the oral hearing. In addition, we understand India not to disagree that developing countries may have different individual needs, given that it argues that paragraph 3(c) should be interpreted as requiring "GSP schemes [to] respond to the needs of developing countries as a whole and not their individual needs." (India's appellee's submission, para. 124)

<sup>333</sup>Enabling Clause, para. 1 (attached as Annex 2 to this Report).

<sup>334</sup>*WTO Agreement*, Preamble, second recital.

<sup>335</sup>*WTO Agreement*, Preamble, first recital.

an *objective* standard. Broad-based recognition of a particular need, set out in the *WTO Agreement* or in multilateral instruments adopted by international organizations, could serve as such a standard.<sup>336</sup>

164. Secondly, paragraph 3(c) mandates that the response provided to the needs of developing countries be "positive". "Positive" is defined as "consisting in or characterized by constructive action or attitudes".<sup>337</sup> This suggests that the response of a preference-granting country must be taken with a view to *improving* the development, financial or trade situation of a beneficiary country, based on the particular need at issue. As such, in our view, 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 paragraph 2, and, on the other hand, 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. Therefore, only if a preference-granting country acts in the "positive" manner suggested, in "respon[se]" to a widely-recognized "development, financial [or] trade need", can such action satisfy the requirements of paragraph 3(c).

165. Accordingly, we are of the view that, by requiring developed countries to "respond positively" to the "needs of developing countries", which are varied and not homogeneous, paragraph 3(c) indicates that a GSP scheme may be "non-discriminatory" even if "identical" tariff treatment is not accorded to "all" GSP beneficiaries. Moreover, paragraph 3(c) suggests that tariff preferences under GSP schemes may be "non-discriminatory" when the relevant tariff preferences are addressed to a particular "development, financial [or] trade need" and are made available to all beneficiaries that share that need.

166. India submits that developing countries should not be presumed to have waived their MFN rights under Article I:1 of the GATT 1994 *vis-à-vis* other developing countries<sup>338</sup>, and we make no such presumption. In fact, we note that the Enabling Clause *specifically* allows developed countries to provide differential and more favourable treatment to developing countries "notwithstanding" the provisions of Article I.<sup>339</sup> With this in mind, and given that paragraph 3(c) of the Enabling Clause contemplates, in certain circumstances, differentiation among GSP beneficiaries, we cannot agree with India that the right to MFN treatment can be invoked by a GSP beneficiary *vis-à-vis* other GSP beneficiaries in the context of GSP schemes that meet the conditions set out in the Enabling Clause.

167. Finally, we note that, pursuant to paragraph 3(a) of the Enabling Clause, any "differential and more favourable treatment ... shall be designed to facilitate and promote the trade of developing countries and not to raise barriers to or create undue difficulties for the trade of any other contracting parties." This requirement applies, *a fortiori*, to any preferential treatment

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<sup>336</sup>The European Communities argues that tariff preferences are an appropriate response to the drug problem. In support of its argument, the European Communities refers to the Preamble to the *Agreement on Agriculture* and the waiver for the United States' Andean Trade Preference Act. In addition, the European Communities finds support in several international conventions and resolutions that have recognized drug production and drug trafficking as entailing particular problems for developing countries. (See Panel Report, paras. 4.71-4.74; and European Communities' appellant's submission, paras. 144-149)

<sup>337</sup>*Shorter Oxford English Dictionary*, 5th ed., W.R. Trumble, A. Stevenson (eds.) (Oxford University Press, 2002), Vol. 2, p. 2293.

<sup>338</sup>India's appellee's submission, para. 94.

<sup>339</sup>Compare para. 1 of the Enabling Clause ("Notwithstanding the provisions of Article I") with para. (a) of the 1971 Waiver Decision ("the provisions of Article I shall be waived ... to the extent necessary").

granted to one GSP beneficiary that is not granted to another.<sup>340</sup> Thus, although paragraph 2(a) does not prohibit *per se* the granting of different tariff preferences to different GSP beneficiaries<sup>341</sup>, and paragraph 3(c) even contemplates such differentiation under certain circumstances<sup>342</sup>, paragraph 3(a) requires that any positive response of a preference-granting country to the varying needs of developing countries not impose unjustifiable burdens on other Members.

168. Having examined the context of paragraph 2(a), we turn next to examine the object and purpose of the *WTO Agreement*. We note first that paragraph 7 of the Enabling Clause provides that "[t]he concessions and contributions made and the obligations assumed by developed and less-developed contracting parties under the provisions of the [GATT 1994] should promote the basic objectives of the [GATT 1994], including those embodied in the Preamble". As we have observed, the Preamble to the *WTO Agreement* provides that there is "need for positive efforts designed to ensure that developing countries, and especially the least developed among them, secure a share in the growth in international trade commensurate with the needs of their economic development".<sup>343</sup> Similarly, the Preamble to the 1971 Waiver Decision provides that "a principal aim of the CONTRACTING PARTIES is promotion of the trade and export earnings of developing countries for the furtherance of their economic development".<sup>344</sup> These objectives are also reflected in paragraph 3(c) of the Enabling Clause, which states that the treatment provided under the Enabling Clause "shall ... be designed and, if necessary, modified, to respond positively to the development, financial and trade needs of developing countries".

169. Although enhanced market access will contribute to responding to the needs of developing countries *collectively*, we have also recognized that the needs of developing countries may vary over time. We are of the view that the objective of improving developing countries' "share in the growth in international trade", and their "trade and export earnings", can be fulfilled by promoting preferential policies aimed at those interests that developing countries have in common, *as well as* at those interests shared by sub-categories of developing countries based on their particular needs. An interpretation of "non-discriminatory" that does not require the granting of "identical tariff preferences"<sup>345</sup> allows not only for GSP schemes providing preferential market access to all beneficiaries, but also the possibility of additional preferences for developing countries with particular needs, provided that such additional preferences are not inconsistent with other provisions of the Enabling Clause, including the requirements that such preferences be "generalized" and "non-reciprocal". We therefore consider such an interpretation to be consistent with the object and purpose of the *WTO Agreement* and the Enabling Clause.

(...)

174. For all of these reasons, we *reverse* the Panel's finding, in paragraphs 7.161 and 7.176 of the Panel Report, that "the term 'non-discriminatory' in footnote 3 [to paragraph 2(a) of the Enabling Clause] requires that identical tariff preferences under GSP schemes be provided to all

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<sup>340</sup>We note in this respect that the language contained in paragraph 3(a) of the Enabling Clause is reflected in waivers referred to in *supra*, footnote **Error! Bookmark not defined.**

<sup>341</sup>*Supra*, paras. **Error! Reference source not found.**-0.

<sup>342</sup>*Supra*, paras. 0-**Error! Reference source not found.**

<sup>343</sup>*WTO Agreement*, Preamble, second recital.

<sup>344</sup>1971 Waiver Decision, Preamble, first recital.

<sup>345</sup>Panel Report, para. 7.161.

developing countries without differentiation, except for the implementation of a priori limitations."<sup>346</sup>

(...)

### C. Consistency of the Drug Arrangements with the Enabling Clause

177. We turn next to examine the consistency of the Drug Arrangements with the Enabling Clause.

178. We recall that, with respect to the Enabling Clause, the only challenge by India before the Panel related to paragraph 2(a) and, in particular, footnote 3 thereto.<sup>347</sup> In response, the European Communities argued that it found contextual support for its interpretation of paragraph 2(a) in the requirement, contained in paragraph 3(c), to respond positively to the needs of developing countries.<sup>348</sup> In rejecting the European Communities' interpretation of paragraph 2(a), the Panel did not determine whether the Drug Arrangements satisfy the conditions set out in paragraph 3(c), but, rather, limited its discussion of paragraph 3(c) to the relevance of that provision as context for its interpretation of paragraph 2(a). Thus, the Panel made a finding of inconsistency only with respect to paragraph 2(a) of the Enabling Clause.<sup>349</sup> The European Communities appeals this finding of inconsistency with paragraph 2(a).

179. Although paragraph 3(c) informs the interpretation of the term "non-discriminatory" in footnote 3 to paragraph 2(a), as detailed above<sup>350</sup>, paragraph 3(c) imposes requirements that are separate and distinct from those of paragraph 2(a). We have already concluded that, where a developed-country Member provides additional tariff preferences under its GSP scheme to respond positively to widely-recognized "development, financial and trade needs" of developing countries within the meaning of paragraph 3(c) of the Enabling Clause, this "positive response" would not, as such, fail to comply with the "non-discriminatory" requirement in footnote 3 of the Enabling Clause<sup>351</sup>, even if such needs were not common or shared by all developing countries. We have also observed that paragraph 3(a) requires that any positive response of a preference-granting country to the varying needs of developing countries not impose unjustifiable burdens on other Members.<sup>352</sup> With these considerations in mind, and recalling that the Panel made no finding in this case as to whether the Drug Arrangements are inconsistent with paragraphs 3(a) and 3(c) of the Enabling Clause<sup>353</sup>, we limit our analysis here to paragraph 2(a) and do not examine *per se* whether the Drug Arrangements are consistent with the obligation contained in paragraph 3(c) to "respond positively to the development, financial and trade needs of developing countries" or with the obligation contained in paragraph 3(a) not to "raise barriers" or "create undue difficulties" for the trade of other Members.

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<sup>346</sup>Given our interpretation, which permits differentiation among GSP beneficiaries, it is not necessary for us to rule on whether *a priori* limitations are permitted under the Enabling Clause. (See also, *supra*, paras. **Error! Reference source not found.-Error! Reference source not found.**)

<sup>347</sup>*Supra*, paras. **Error! Reference source not found.-Error! Reference source not found.**

<sup>348</sup>See Panel Report, para. 7.123; European Communities' first written submission to the Panel, paras. 70-71 and 149; and European Communities' second written submission to the Panel, paras. 48-52.

<sup>349</sup>Panel Report, para. 8.1(d).

<sup>350</sup>*Supra*, paras. 0-0.

<sup>351</sup>*Supra*, para. **Error! Reference source not found.**

<sup>352</sup>*Supra*, para. 0.

<sup>353</sup>See *supra*, para. **Error! Reference source not found.**

180. We found above that the term "non-discriminatory" in footnote 3 to paragraph 2(a) of the Enabling Clause does not prohibit the granting of different tariffs to products originating in different sub-categories of GSP beneficiaries, but that identical tariff treatment must be available to all GSP beneficiaries with the "development, financial [or] trade need" to which the differential treatment is intended to respond.<sup>354</sup> The need alleged to be addressed by the European Communities' differential tariff treatment is the problem of illicit drug production and trafficking in certain GSP beneficiaries. In the context of this case, therefore, the Drug Arrangements may be found consistent with the "non-discriminatory" requirement in footnote 3 only if the European Communities proves, at a minimum, that the preferences granted under the Drug Arrangements are available to all GSP beneficiaries that are similarly affected by the drug problem.<sup>355</sup> We do not believe this to be the case.

181. By their very terms, the Drug Arrangements are limited to the 12 developing countries designated as beneficiaries in Annex I to the Regulation.<sup>356</sup> Specifically, Article 10.1 of the Regulation states:

Common Customs Tariff *ad valorem* duties on [covered products] which originate in a country that according to Column I of Annex I benefits from [the Drug Arrangements] shall be entirely suspended.

182. Articles 10 and 25 of the Regulation, which relate specifically to the Drug Arrangements, provide no mechanism under which additional beneficiaries may be added to the list of beneficiaries under the Drug Arrangements as designated in Annex I. Nor does any of the other Articles of the Regulation point to the existence of such a mechanism with respect to the Drug Arrangements. Moreover, the European Communities acknowledged the absence of such a mechanism in response to our questioning at the oral hearing. This contrasts with the position under the "special incentive arrangements for the protection of labour rights" and the "special incentive arrangements for the protection of the environment", which are described in Article 8 of the Regulation. The Regulation includes detailed provisions setting out the procedure and substantive criteria that apply to a request by a beneficiary under the general arrangements described in Article 7 of the Regulation (the "General Arrangements") to become a beneficiary under either of those special incentive arrangements.<sup>357</sup>

182. What is more, the Drug Arrangements themselves do *not* set out any clear prerequisites—or "objective criteria"<sup>358</sup>—that, if met, would allow for other developing countries "that are similarly affected by the drug problem"<sup>359</sup> to be *included* as beneficiaries under the Drug Arrangements.<sup>360</sup> Indeed, the European Commission's own Explanatory Memorandum notes that

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<sup>354</sup>*Supra*, para. **Error! Reference source not found.**

<sup>355</sup>According to the European Communities, "the Drug Arrangements are *non-discriminatory* because the designation of the beneficiary countries is based only and exclusively on their development needs. All the developing countries that are similarly affected by the drug problem have been included in the Drug Arrangements". (European Communities' appellant's submission, para. 186 (original italics))

<sup>356</sup>The 12 designated beneficiary countries are: Bolivia, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Honduras, Nicaragua, Pakistan, Panama, Peru, and Venezuela. (Regulation, Annex I (Column I))

<sup>357</sup>Regulation, Title III.

<sup>358</sup>European Communities' appellant's submission, paras. 4 and 139.

<sup>359</sup>*Ibid.*, para. 186.

<sup>360</sup>In response to Question 4 posed by India at the First Panel Meeting, the European Communities confirmed that the Regulation does not set out objective criteria for designating beneficiary countries under

"the benefits of the drug regime ... are given without *any* prerequisite."<sup>361</sup> Similarly, the Regulation offers no criteria according to which a beneficiary could be *removed* specifically from the Drug Arrangements on the basis that it is no longer "similarly affected by the drug problem". Indeed, Article 25.3 expressly states that the evaluation of the effects of the Drug Arrangements described in Articles 25.1(b) and 25.2 "will be without prejudice to the continuation of the [Drug Arrangements] until 2004, and their possible extension thereafter." This implies that, even if the European Commission found that the Drug Arrangements were having no effect whatsoever on a beneficiary's "efforts in combating drug production and trafficking"<sup>362</sup>, or that a beneficiary was no longer suffering from the drug problem, beneficiary status would continue.<sup>363</sup> Therefore, even if the Regulation allowed for the list of beneficiaries under the Drug Arrangements to be modified, the Regulation 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" on a particular country. In addition, we note that the Regulation does not, for instance, provide any indication as to how the European Communities would assess whether the Drug Arrangements provide an "adequate and proportionate response"<sup>364</sup> to the needs of developing countries suffering from the drug problem.

184. It is true that a country may be removed as a beneficiary under Annex I, either altogether or in respect of certain product sectors, for reasons that are not specific to the Drug Arrangements. Thus, Article 3 of the Regulation provides for the removal of a country from Annex I (and hence, from the General Arrangements and any other arrangements under which it is a beneficiary) if particular circumstances are met indicating that the country has reached a certain level of development. Article 12 provides for the removal of a country as a beneficiary under the General Arrangements and the Drug Arrangements with respect to a product sector where the country's level of development and competition has reached a certain threshold with respect to that sector. Neither Article 3 nor Article 12 appears to relate in any way to the degree to which the country is suffering from the "drug problem". Finally, Title V to the Regulation contains certain "Temporary Withdrawal and Safeguard Provisions" that are common to all the preferential arrangements under the Regulation. Although one reason for which the arrangements may be temporarily withdrawn is "shortcomings in customs controls on export or transit of drugs (illicit substances or precursors), or failure to comply with international conventions on money laundering"<sup>365</sup>, this reason applies equally to the General Arrangements, the Drug Arrangements, and the other special incentive arrangements. Moreover, as the Panel appeared to recognize, this

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the Drug Arrangements. The European Communities stated:

The criteria are not set out in the GSP Regulation. They are not contained in a public document.

(Panel Report, p. B-69, para. 5)

<sup>361</sup>Explanatory Memorandum to the Proposal for a Council Regulation applying a scheme of generalised tariff preferences for the period 1 January 2002 to 31 December 2004, para. 35 (emphasis added) (attached to Amended Proposal for a Council Regulation applying a scheme of generalised tariff preferences for the period 1 January 2002 to 31 December 2004, 2001/0131 (ACC), at p. 3) (Exhibit India-7 submitted by India to the Panel).

<sup>362</sup>Regulation, Art. 25.1(b).

<sup>363</sup>In response to questioning at the oral hearing, the European Communities confirmed that, although the sixth recital to the Preamble of the Regulation provides that the Drug Arrangements "should be closely monitored", the list of beneficiaries will be unaffected by the monitoring described in Articles 25.1 and 25.2 of the Regulation.

<sup>364</sup>European Communities' appellant's submission, para. 133.

<sup>365</sup>Regulation, Art. 26.1(d).

condition is not connected to the question of whether the beneficiary is a "seriously drug-affected country".<sup>366</sup>

185. We note, moreover, that the Drug Arrangements will be in effect until 31 December 2004.<sup>367</sup> Until that time, other developing countries that are "similarly affected by the drug problem" can be included as beneficiaries under the Drug Arrangements only through an amendment to the Regulation. The European Communities confirmed this understanding in response to questioning at the oral hearing.

186. Against this background, we fail to see how the Drug Arrangements can be distinguished from other schemes that the European Communities describes as "confined *ab initio* and permanently to a limited number of developing countries".<sup>368</sup> As we understand it, the European Communities' position is that such schemes would be discriminatory, whereas the Drug Arrangements are not because "all developing countries are potentially beneficiaries" thereof.<sup>369</sup> In seeking a waiver from its obligations under Article I:1 of the GATT 1994 to implement the Drug Arrangements, the European Communities explicitly acknowledged, however, that "[b]ecause the special arrangements *are only available* to imports originating in [the 12 beneficiaries of the Drug Arrangements], a waiver ... appears necessary".<sup>370</sup> This statement appears to undermine the European Communities' argument that "all developing countries are potentially beneficiaries of the Drug Arrangements" and, therefore, that the Drug Arrangements are "non-discriminatory".<sup>371</sup>

187. We recall our conclusion that the term "non-discriminatory" in footnote 3 of the Enabling Clause requires that identical tariff treatment be available to all similarly-situated GSP beneficiaries. We find that the measure at issue fails to meet this requirement for the following reasons. First, as the European Communities itself acknowledges, according benefits under the Drug Arrangements to countries other than the 12 identified beneficiaries would require an amendment to the Regulation. Such a "closed list" of beneficiaries cannot ensure that the preferences under the Drug Arrangements are available to all GSP beneficiaries suffering from illicit drug production and trafficking.

188. Secondly, the Regulation contains no criteria or standards to provide a basis for distinguishing beneficiaries under the Drug Arrangements from other GSP beneficiaries. Nor did the European Communities point to any such criteria or standards anywhere else, despite the Panel's request to do so.<sup>372</sup> As such, the European Communities cannot justify the Regulation under paragraph 2(a), because it does not provide a basis for establishing whether or not a developing country qualifies for preferences under the Drug Arrangements. Thus, although the European Communities claims that the Drug Arrangements are available to all developing

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<sup>366</sup>Panel Report, para. 7.216.

<sup>367</sup>Regulation, Arts. 1.1 and 41.2. We understand that the Regulation has been extended to 31 December 2005. (Council Regulation (EC) No. 2211/2003 of 15 December 2003 amending Regulation (EC) No. 2501/2001 applying a scheme of generalised tariff preferences for the period from 1 January 2002 to 31 December 2004 and extending it to 31 December 2005, *Official Journal of the European Union*, L Series, No. 332 (19 December 2003), p. 1)

<sup>368</sup>European Communities' appellant's submission, para. 185.

<sup>369</sup>*Ibid.*, para. 186.

<sup>370</sup>Council for Trade in Goods, Request for a WTO Waiver, *New EC Special Tariff Arrangements to Combat Drug Production and Trafficking*, G/C/W/328, 24 October 2001, p. 2. (emphasis added)

<sup>371</sup>European Communities' appellant's submission, para. 186.

<sup>372</sup>See *supra*, footnote 360.

countries that are "similarly affected by the drug problem"<sup>373</sup>, because the Regulation does not define the criteria or standards that a developing country must meet to qualify for preferences under the Drug Arrangements, there is no basis to determine whether those criteria or standards are discriminatory or not.

189. For all these reasons, we find that the European Communities has failed to prove that the Drug Arrangements meet the requirement in footnote 3 that they be "non-discriminatory". Accordingly, we *uphold*, for different reasons, the Panel's conclusion, in paragraph 8.1(d) of the Panel Report, that the European Communities "failed to demonstrate that the Drug Arrangements are justified under paragraph 2(a) of the Enabling Clause".

## VI. Findings and Conclusions

190. For the reasons set out in this Report, the Appellate Body:

- (a) upholds the Panel's finding, in paragraph 7.53 of the Panel Report, that the Enabling Clause is an "exception" to Article I:1 of the GATT 1994;
- (b) upholds the Panel's finding, in paragraph 7.53 of the Panel Report, that the Enabling Clause "does not exclude the applicability" of Article I:1 of the GATT 1994;
- (c) modifies the Panel's finding, in paragraph 7.53 of the Panel Report, that the European Communities "bears the burden of invoking the Enabling Clause and justifying its Drug Arrangements" under that Clause, by finding that it was incumbent upon India to *raise* the Enabling Clause in making its claim of inconsistency with Article I:1 of the GATT 1994, but that the European Communities bore the burden of *proving* that the Drug Arrangements satisfy the conditions of the Enabling Clause, in order to justify those Arrangements under that Clause; and finds, further, that India sufficiently raised paragraph 2(a) of the Enabling Clause in making its claim of inconsistency with Article I:1 before the Panel;
- (d) need not rule on the Panel's conclusion, in paragraphs 7.60 and 8.1(b) of the Panel Report, that the Drug Arrangements are inconsistent with Article I:1 of the GATT 1994;
- (e) reverses the Panel's finding, in paragraphs 7.161 and 7.176 of the Panel Report, that "the term 'non-discriminatory' in footnote 3 [to paragraph 2(a) of the Enabling Clause] requires that identical tariff preferences under GSP schemes be provided to all developing countries without differentiation, except for the implementation of a priori limitations";
- (f) reverses the Panel's finding, in paragraph 7.174 of the Panel Report, that "the term 'developing countries' in paragraph 2(a) [of the Enabling Clause] should be interpreted to mean *all* developing countries, with the exception that where developed countries are implementing a priori limitations, 'developing countries' may mean *less than all* developing countries"; and

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<sup>373</sup>European Communities' appellant's submission, para. 186.

- (g) upholds, for different reasons, the Panel's conclusion, in paragraph 8.1(d) of the Panel Report, that the European Communities "failed to demonstrate that the Drug Arrangements are justified under paragraph 2(a) of the Enabling Clause".

199. The Appellate Body therefore recommends that the Dispute Settlement Body request the European Communities to bring Council Regulation (EC) No. 2501/2001, found in this Report, and in the Panel Report as modified by this Report, to be inconsistent with Article I:1 of the GATT 1994 and not justified under paragraph 2(a) of the Enabling Clause, into conformity with its obligations under the GATT 1994.

### 3. Optional Reading

**R E Hudec, "Like Product": The Difference in Meaning in GATT Articles I and III in: Cottier/Mavroidis (eds) Regulatory Barriers and the Principle of Non-Discrimination in World Trade Law, 2000, 101-123.**

**European Communities – Customs Classification of Frozen Boneless Chicken Cuts (EC – Chicken Cuts)**

WT/DS269/AB/R, WT/DS286/AB/R, Appellate Body Report circulated on 12 September 2005 ([http://www.wto.org/english/tratop\\_e/dispu\\_e/cases\\_e/ds286\\_e.htm](http://www.wto.org/english/tratop_e/dispu_e/cases_e/ds286_e.htm))

272. We agree with the Panel that, in general, agreement may be deduced from the affirmative reaction of a treaty party. However, we have misgivings about deducing, *without further inquiry*, agreement with a practice from a party's "lack of reaction". We do not exclude that, in specific situations, the "lack of reaction" or silence by a particular treaty party may, in the light of attendant circumstances, be understood as acceptance of the practice of other treaty parties.<sup>374</sup> (...) Therefore, the fact that Brazil and Thailand, having actually exported the products at issue, may have accepted the European Communities' import classification practice under heading 02.10, is not dispositive of

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<sup>374</sup>"It is not necessary to show that each party has engaged in a practice, only that all have accepted it, albeit tacitly." (A. Aust, *Modern Treaty Law and Practice* (Cambridge University Press, 2000), p. 195) See also D. Anzilotti, *Corso di Diritto Internazionale* ["International Law Course"], Vol. 1, IV Edizione (CEDAM, 1955), p. 292:

These conclusive facts also include silence, the value of which, as a manifestation of will, obviously cannot be reduced to general rules, because such value depends on the factual circumstances in which the silence is observed ... It is easy, moreover, to envisage circumstances in which silence on the part of a State cannot be construed as anything but indifference or failure to express its will in any form: The recently expressed view that, in international law, the principle of *qui tacet consentire videtur* is entirely valid cannot be accepted in such general terms[.].

(Unofficial English translation from available French translation by G. Gidel, *Cours de droit international*, Vol. 1, III édition (Librairie du Recueil Sirey, 1929), p. 344);

J.P. Cot, "La Conduite subséquente des Parties à un traité" ["Subsequent Conduct of the Parties to a Treaty"], in *Revue Générale de Droit International Public* (1966), 3rd series, Vol. 37, p. 645:

... the various facets of the subsequent conduct of the Parties in the law of treaties: Where it is the subject of tacit agreement, subsequent conduct should undoubtedly be approved by all the Parties; on the other hand, where it is merely indicative of the will of the Parties, it may be accepted even if it stems from a single State. *Its probative value then depends on the circumstances of the case.*

(Unofficial English translation; emphasis added);

W. Karl, *Vertrag und spätere Praxis im Völkerrecht* ["Treaty and Subsequent Practice in International Law"] (Springer Verlag, 1983), pp. 113 and 127; and F. Capotorti, "Sul Valore della Prassi Applicativa dei Trattati Secondo la Convenzione di Vienna" ["On the Value of Practice in the Application of Treaties under the Vienna Convention"], in *Le Droit international à l'heure de sa codification*, Studi in onore di Roberto Ago (Giuffrè, 1987), Vol. I, pp. 197.

whether other Members with actual or potential trade interests have also accepted that practice. We, therefore, disagree with the Panel that "subsequent practice" under Article 31(3)(b) has been established by virtue of the fact that the Panel "[had] not been provided any evidence to indicate that WTO Members protested against the EC classification practice in question from 1996 - 2002".<sup>375</sup>

[Footnote numbering is different from the original.]

**European Communities – Selected Custom Matters,**

WT/DS315/AB/R, Appellate Body Report circulated on Nov. 13, 2006

([http://www.wto.org/english/tratop\\_e/dispu\\_e/cases\\_e/ds315\\_e.htm](http://www.wto.org/english/tratop_e/dispu_e/cases_e/ds315_e.htm))

The AB concluded that the Panel did not find that Article X:3(a) of the GATT 1994 requires uniformity of “administrative processes”; upheld the Panel's finding that the term “administer” in Article X:3(a) of the GATT 1994 may include administrative processes that put into effect the legal instruments of the kind described in Article X:1 of the GATT 1994; but reversed the Panel's finding that the administrative process leading to the tariff classification of blackout drapery lining amounts to non-uniform administration within the meaning of Article X:3(a) of the GATT 1994, and that the European Communities has violated Article X:3(a) of the GATT 1994 with respect to the tariff classification of blackout drapery lining; (...)

[From the WTO website]

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<sup>375</sup>Panel Reports, para. 7.255.