

*European Communities – Conditions for the Granting of Preferences to
Developing Countries*

(WT/DS246)

**Third Party Submission of
Paraguay**

**Geneva
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I. INTRODUCTION

1. Paraguay welcomes this opportunity to express its views in this dispute concerning the WTO-consistency of the Special Incentive Arrangements to Combat Drug Production and Trafficking (the "Drug Arrangements") as set out in Council Regulation EC (No) 2501/2001 (the "Regulation") of the European Communities ("EC").

2. Paraguay has a substantial interest in this matter from two distinct standpoints. First, the matter before the Panel involves systemic issues that have a significant bearing on the interpretation and application of basic principles of the multilateral trading system, particularly the most-favoured-nation-treatment obligation ("MFN") and the proper application of the provisions concerning Special and Differential Treatment (S&D) to developing countries. It is in Paraguay's interest that the Panel does not create exceptions from the MFN principle that have not been negotiated among Members and preserves the rights and obligations of Members as stipulated in Article 3.2 of the Understanding on Rules and Procedures Governing the Settlement of Disputes ("DSU").

3. On a more specific level, Paraguay has a particular interest in this dispute as one of the developing country Members adversely affected by the Drug Arrangements. Tariff preferences granted to some developing countries adversely affect the exports of all developing countries excluded from the tariff preferences. To that extent, the "cost" of the preferences granted to a limited group of developing countries is borne by the developing countries excluded from the Drug Arrangements, including Paraguay.

4. Paraguay has suffered and continues to suffer from the discriminatory treatment accorded by the EC. Paraguay has consistently maintained in various fora of the WTO that tariff preferences accorded to developing countries under the Enabling Clause must, in accordance with its terms, be formulated and applied in a "generalized, non-reciprocal and non-discriminatory" manner.

II. SYSTEMIC CONCERNS

A. *The elimination of discrimination is a primary objective of the multilateral trading system*

5. One of the primary objectives of the Agreement Establishing the World Trade Organisation ("WTO Agreement"), as stated in its preamble, is "the elimination of discriminatory treatment in international relations".

6. The elimination of discriminatory treatment is a fundamental element of the rules of the multilateral trading system. The interpreter of the WTO Agreement must therefore assume that the principle of non-discrimination applies unless the Members of the WTO ("Members") have explicitly and clearly agreed otherwise. Any departure from the MFN principle entails trade benefits for some and trade losses for others, and thereby modifies the negotiated balance of rights and obligations. Any departure from this principle can therefore only result from negotiations among Members. The Members of the WTO have never agreed that the developed countries may grant tariff preferences to a selected group of developing countries. The EC has sought the required agreement by requesting a waiver but has failed to obtain it. The Drug Arrangements have therefore remained unilateral and consequently WTO-inconsistent departures from the MFN principle.

B. *The issue of discrimination on the basis of "objective criteria" is not a matter before the Panel*

7. The EC and India agree that under the Decision of 28 November 1979 on "Differential and More Favourable Treatment Reciprocity and Fuller Participation of Developing Countries (the "Enabling Clause"), preferential tariff treatment under the Generalized System of Preferences ("GSP") must be "non-discriminatory"; however they differ in their interpretations of this term. The EC alleges that the Enabling Clause permits developed countries to treat differently "developing countries which, according to objective criteria have different development needs."¹

8. This argument is not pertinent to the measures India decided to submit to the Panel.

¹ Para 84 of the EC submission.

9. The measures at issue are the Drug Arrangements as set out in the Regulation. Unlike the provisions governing the special incentive arrangements for the protection of labour rights or the special incentive arrangements for the protection of the environment, the provisions of the Regulation establishing the Drug Arrangements do not establish (i) any "objective criteria" for the inclusion of developing countries in the Drug Arrangements nor (ii) any procedure or criteria for their inclusion. The provisions simply state that a group of named countries are entitled to special preferences. Paraguay is not part of that group and nowhere does the Regulation state which "objective criteria" Paraguay would have to meet to become part of that group. The plain fact is that the incentives under the Drug Arrangements are confined to specific beneficiaries pre-designated by the EC, not to countries meeting certain criteria.

10. The measures at issue thus discriminate in favour of specified countries, not in favour of countries meeting defined criteria. The question of whether the Enabling Clause permits the EC to adopt GSP schemes that discriminate between developing countries on the basis of objective criteria is therefore not a matter before the Panel for purposes of Article 11 of the DSU. In any case, as elaborated below, the Enabling Clause does not authorize differentiation in treatment between developing countries.

C. *The Enabling Clause in any case does not permit differentiation in treatment between developing countries in the context of GSP schemes*

11. All developing countries have different development needs. The Enabling Clause does not permit developed countries to grant differential treatment to some developing countries on the basis that they have "different development needs". If this were the case, there would be no need to explicitly provide for Paragraph 2(d) of the Enabling Clause, which specifically authorises "*special treatment of the least developed* among the developing countries in the context of any general or specific measures in favour of developing countries". Thus, discrimination between developing countries is envisaged only for the least developed countries, not for any group of developing countries having "different development needs", whether least developed or not. It is not sufficient for the EC to assert that its criterion for differentiation is "justified", it must show that the criterion for differentiation used by it is expressly envisaged under the Enabling Clause. It has manifestly failed to do so in the present case.

12. Not only is the EC's interpretation contradicted by Paragraph 2(d) of the Enabling Clause. It also runs contrary to the agreement reached between developing and developed countries in the context of the UNCTAD reflected in Paragraph 2(a) of the Enabling Clause. Paragraph 2(a) limits the scope of departure from Article I of GATT 1994 solely to preferential tariff treatment which is in accordance with the "Generalized System of Preferences"... as described in the "Decision of the Contracting Parties of 25 June 1971" (the 1971 Waiver"). The 1971 Waiver authorizes a waiver from Article I:1 to allow "developed contracting parties ... to accord preferential treatment to products originating in developing countries and territories *generally the preferential tariff treatment referred to in the Preamble to this Decision*". The preamble in turn states:

“... *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 in 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 ... (emphasis supplied)

13. The Mutually Acceptable Arrangements drawn up in UNCTAD are contained in the “Agreed Conclusions of the Special Committee on Preferences”² (“Agreed Conclusions”) adopted by the Trade and Development Board on 13 October 1970. The Agreed Conclusions represent the outcome of negotiations held over a period of over two years pursuant to Resolution 21 (II) of the Second Conference held in New Delhi.

14. Under the EC's interpretation, sub-groups of developing countries can be singled out for preferential treatment as long as "according to objective criteria they have different development needs", which implies that developed country members can unilaterally determine those criteria. However, under the Agreed Conclusions, no such flexibility was

² Report of the Special Committee on Preferences on the second part of its fourth session, 21-September – 12 October 1970 (TD/B/AC.5/36/Rev.1).

envisaged. They merely envisaged that the developed countries could (i) utilise "safeguard mechanisms"³ and (ii) arguably, exclude certain countries from beneficiary status altogether.⁴ However, there is absolutely no reference to the notion that the developed countries should be able to distinguish between the countries that they have recognised to be developing countries. This is also clear from Part V of the Agreed Conclusions which expressly refers to "Special Measures in Favour of the Least Developed Among the Developing Countries". No further basis for differential treatment between developing countries was envisaged.

15. On the EC's reading of the Enabling Clause, it is possible to grant tariff preferences to a set of developing countries without granting the same tariff preferences to least developed countries, as long as the set of developing countries have distinct development needs. This illustrates the difficulty with the standard proposed by the EC. Least developed countries could experience trade diversion to developing countries merely because these favoured developing countries have a "developmental need" considered to be especially pressing by a developed country. In the present case, it is difficulties faced on account of drug production and trafficking; but in others it could be, for example, "transition from military rule", "high population growth", "literacy rate", "high levels of corruption", or "degree of rural electrification". While developing countries have a variety of developmental needs; the Enabling Clause does not allow developed country Members to pick and choose amongst these needs in granting tariff preferences. Instead, it envisages one uncontroversial category of permissible differentiation in favour of the countries determined by the United Nations to be the most needy - special treatment for least developed countries. The EC fails to explain how the developmental problems of countries confronting drug production and trafficking are unique and more pressing than the developmental problems faced by other developing countries on account of a host of other factors.

16. The implication of the EC's approach is that developed countries could manipulate the GSP system so as to pursue their own political agenda and that the rule-based character of the multilateral trading system would be completely undermined. In this context, it is important to point out that the rules-based multilateral trading system was established precisely to ensure a level playing field in which all Members, regardless of level of economic

³ Part III of the Agreed Conclusions.

⁴ Part IV of the Agreed Conclusions.

development or political power, conduct their trade relations in accordance with rules and norms established by the Members themselves acting through the WTO. The EC's approach further exacerbates the intrinsic disadvantages of developing countries.

17. It is clear that the discriminatory nature of the Drug Arrangements results in obstacles to exports of the developing countries discriminated against. The Drug Arrangements have pernicious effects on current exports and also impede the creation of future trade opportunities. Any assessment of the measures before the Panel must take into account the need of investors and traders for clear and predictable rules permitting them to plan their activities. Creating the possibility for developed countries to distinguish between the developing countries on the basis of unilaterally determined criteria would remove all predictability in the trade relations between developed and developing countries.

18. The EC's interpretation of the concept of non-discrimination cannot therefore be reconciled with Paragraph 3(a) of the Enabling Clause, which mandates that GSP schemes "shall be designed to facilitate and *promote* the trade of developing countries". Nor can it be reconciled with the requirements of Paragraph 3(c) of the Enabling Clause which stipulates that GSP schemes shall be designed to respond positively to the "trade needs" of developing countries.

D. *The Waiver mechanism provides the required flexibility*

19. If Members wish to implement discriminatory measures inconsistent with their obligations under the WTO Agreement, they may do so only by resorting to Article IX of the WTO Agreement. Article IX of the WTO Agreement provides them with the flexibility to deviate from their WTO obligations. The waiver procedures give potentially affected Member the opportunity to redress any adverse effect of preferences favouring a group of countries by negotiating compensatory market access commitments. In this way, Article IX limits the damage caused to other Members by measures which are not consistent with the provisions of the WTO Agreement.

20. In 1976, Paraguay was affected by the special and differential treatment granted only to ACP Countries under the Lomé Convention. Nonetheless, the EC resorted to the waiver mechanism in order to obtain the consent of the membership and redress the damage to the

affected developing countries. As a result, other Members, including Paraguay, were given the opportunity to request compensatory concessions from the EC.

21. The present situation is completely different. By unilaterally proceeding to implement the Drug Arrangements without the benefit of a waiver, the EC has disregarded the multilateral nature of the WTO system and has deprived Paraguay and other developing country Members of the opportunity to mitigate the damage created by the discriminatory character of the Drug Arrangements.

III. CONCERNS SPECIFIC TO THE SITUATION OF PARAGUAY

22. Many developing countries which face drug problems are excluded from the coverage of the Drug Arrangements. The EC has even referred to some of these countries in paragraph 140 of its submission. As far as Paraguay is concerned, due to its specific geographical location, Paraguay faces severe drug trafficking problems. Paraguay's government and society are engaged in combating this problem. Considerable resources have had to be reallocated from other social endeavours in order to deal with it. The situation of Paraguay in terms of drug trafficking is comparable to that of some of the countries included as beneficiaries under the Drug Arrangements. Yet, Paraguay has not been included in the Drug Arrangements, which calls into question the EC's claim that the designation of beneficiary countries of the Drug Arrangements is "made in accordance with objective, non-discriminatory criteria".⁵

23. The Drug Arrangements have caused trade diversion since its inception in 1990. Prior to 1990, several Paraguayan goods were competitive export commodities to the EC. After the introduction of the Drug Arrangements, exports of these products from Paraguay to the EC have considerably declined. In contrast, exports of like products from some of the beneficiary countries have risen. Thus, the implementation of the Drug Arrangements has resulted in trade diversion in favour of the beneficiary countries.

24. Paraguayan enterprises are at a competitive disadvantage *vis-à-vis* their competitors in the beneficiary countries not only because they are denied equivalent market access opportunities. They also have to bear the cost of combating drug trafficking (through internal

⁵ Para 116 of the EC submission.

taxes). Even within Paraguay's domestic market, the negative effects of the tariff preferences are felt. While several of Paraguay's products cannot enter the EC because of the competitive disadvantages resulting from the tariff preferences under the Drug Arrangements, producers in the beneficiary countries are able to enhance their export capacity and thereby attain economies of scale in production. Paraguayan producers are unable to attain similar economies of scale. As a result, producers in other beneficiary countries have enhanced their competitive position *vis-à-vis* Paraguayan producers even in the Paraguayan domestic market.

25. Not only is there trade diversion both in the EC market and in the Paraguayan domestic market. As a result of the discriminatory tariff preferences under the Drug Arrangements, there has also been an "investment diversion". The proximity between Paraguay and some of the beneficiary countries creates the incentive to shift investments away from Paraguay and towards these countries. Moreover, international investment flows in sectors benefiting from the Drug Arrangements are diverted away from Paraguay.

26. The damage that the implementation of the Drug Arrangements has caused to Paraguay is exacerbated by the particularities of the geographical location of Paraguay. As a land-locked nation, Paraguay has to bear higher transport costs in order to export its products to the EC. The development of Paraguay is critically affected by this factor. On the EC's reading of the Enabling Clause, a GSP truly responsive to the needs of development can therefore not focus exclusively on the problems specific to a selected group of countries. It must take into account the considerable variety of problems facing the developing countries and therefore create benefits for all of them.

IV. CONCLUSION

27. The Drug Arrangements are inconsistent with the requirements of the MFN obligation under Article I:1 of the GATT 1994 and are not justified under the Enabling Clause. As a result, Paraguay has suffered from trade and investment diversions.

28. Paraguay requests the Panel to find that the measures at issue are inconsistent with the EC's obligations under the WTO Agreement. In the absence of a waiver agreed upon by the Membership, Paraguay respectfully requests the Panel to suggest to the EC to apply the tariff

preferences under the Drug Arrangements to all developing countries, as contemplated under the Enabling Clause.