Developing Countries in the GATT Legal System

Robert E. Hudec

With a New Introduction by J. Michael Finger

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DEVELOPING COUNTRIES IN THE GATT LEGAL SYSTEM

In this reissued edition of *Developing Countries in the GATT Legal System*, the seminal impact of the late Robert E. Hudec's work on the situation of developing countries within the international trade system is once again available. Robert Hudec is regarded as one of the most prominent commentators on the evolution of the current international trade regime. This book offers his analysis of the dynamics playing out between developed and developing nations. This analysis, insightful when the book was first published, continues to serve as a thoughtful guide to how future trade policy must consider the demands of the developing world.

This edition includes a new introduction by J. Michael Finger that reviews Hudec's work to understand how the General Agreement on Tariffs and Trade (GATT) got into its current historical-institutional predicament. It also examines the lasting impact of Hudec's work on current research on international trade systems.

The late Robert E. Hudec was the Melvin E. Steen Professor of Law at the University of Minnesota. He was a leading authority on trade law and the GATT. During the early stages of the Kennedy Round of multilateral trade negotiations, conducted under the auspices of the GATT, he was Assistant General Counsel to the Special Representative for Trade Negotiations (STR) in the Executive Office of the President of the United States (1963–65), later known as the Executive Office of the President. Professor Hudec wrote many articles in professional journals on the law of international economic affairs. He was the author of *Adjudication of International Trade Disputes* (1977) and *The GATT Legal System and World Trade Diplomacy* (1975).

In memory of Jan Tumlir

Foreword

RELATIONS between developed and developing countries in the international trading system, whose norms, rules and procedures are set out in the General Agreement on Tariffs and Trade (GATT), have been reaching an *impasse*. For a quarter of a century, the developed countries have been allowing, or encouraging, the developing countries to become contracting parties to the GATT without requiring them to abide by the more important obligations of membership. What is more, they have acquiesced in the formal derogation from the principle of non-discrimination, which is the keystone of the GATT, to permit the Generalized System of Preferences (GSP) in favor of developing countries to be established and maintained.

At the same time, developing countries – especially the more advanced ones – have been faced with discriminatory protection against them whenever their exports have been uncomfortably successful in the markets of developed countries, with such protection often taking the form of export-restraint arrangements negotiated "outside" the framework of GATT norms, rules and procedures.

The costs to developing countries of limitations on their access to the markets of developed countries are not so much offset as multiplied by their more or less complete freedom to establish and maintain trade regimes which are highly protectionist and Byzantine in their complexity.

By the early 1980s, it was clear that the role of developing countries in the international trading system was bound to attract increasing attention, especially if a new "round" of multilateral trade negotiations under GATT auspices was to be undertaken. Accordingly, the Trade Policy Research Centre, with the help of a grant from the Leverhulme Trust in London, embarked in 1983 on a major program of studies on the Participation of Developing Countries in the International Trading System, supervised by Martin Wolf, the Centre's Director of Studies.

The purpose of the program has been to clarify, for public discussion and policy formation, the underlying reasons for the current difficulties in relations between developed and developing countries in the GATT system. The program focuses on both economic and legal issues in the GATT system *per se* and on impediments to trade liberalization in individual developing countries. The emphasis on the latter derived from the perception that the GATT framework of norms, rules and procedures can be no more than the "handmaiden" of trade liberalization. Liberalization will not be brought about, however, unless there is a consensus in the countries concerned on both its feasibility and its value in promoting their economic growth and development. The domestic impediments to trade liberalization have to be understood if they are to be overcome.

It is true for all countries that multilateral negotiations are a means more of achieving the trade liberalization that is already widely understood to be in each country's own interests than of liberalizing when no such benefit is seen. In other words, reciprocal bargaining is a way of overcoming domestic resistance to the trade liberalization that is strongly desired by prevailing forces in each country, both in government and in society at large. A desire to liberalize, almost irrespective of what happens elsewhere, is particularly significant in small countries. The smaller the country, the less effective is its international bargaining power and, therefore, the less persuasive is the argument that improved access to markets abroad depends on the liberalization of access to its own market. For this reason, smaller countries usually liberalize only if there is a strong domestic consensus that such liberalization is in their own interests, such a consensus having been long established in countries like Sweden, Switzerland and Singapore.

In developing the program of studies it was clear that both the trade policies of developing countries and the role of those countries in the international trading system reflect economic ideas that have found legal expression in the GATT and associated codes. In particular, developing countries have consistently denied the relevance to themselves of the twin GATT concepts of "equal treatment" and reciprocal trade liberalization. Arguing that "equal treatment of unequals is unfair", developing countries have demanded discrimination in their favor under the general rubric of "special and differential treatment" or, more recently, "differential and more favorable treatment". Arguing that reliance on the market thwarts economic development, developing countries have insisted on their need to introduce protection at home while receiving market access and preferential treatment abroad.

Drafts of the papers arising from the Centre's program of studies were presented at a three-day research meeting at Wiston House, near Steyning, in

the United Kingdom, attended by those engaged on the program and a number of other scholars and officials. The meeting was immediately preceded by a two-day meeting, also at Wiston House, of a study group which is drawing together the conclusions of the program of studies. This meeting, too, was attended by a number of officials. The two international meetings were funded by a grant from the Ford Foundation in New York. As mentioned earlier, the program of studies, as a whole, has been funded by the Leverhulme Trust in London.

As usual, it has to be stressed that the views expressed in this book do not necessarily represent those of members of the Council or those of the staff and associates of the Trade Policy Research Centre which, having general terms of reference, does not represent a consensus of opinion on any particular issue. The purpose of the Centre is to promote independent analysis and public discussion of international economic policy issues.

HUGH CORBET
Director
Trade Policy Research Centre
London
May 1987

Acknowledgments

THE IDEA for this study was conceived by Martin Wolf, Director of Studies at the Trade Policy Research Centre, as part of a program of studies on the Participation of Developing Countries in the International Trading System. An early draft of the study, along with drafts of other studies in the program, was presented at an international conference of scholars and senior officials which the Centre held at Wiston House, near Steyning, West Sussex, England, in October 1984. During the two years it took to bring the study from its Wiston House version to the more ambitious first edition form, Martin functioned as principal editor, critic and motivation coach. With all this assistance came a completely free hand to pursue the issues as I saw fit. To say that I am grateful to Martin and to the Centre would be to state the obvious.

Colleagues who read and commented on earlier typescripts include J. Michael Finger and Robert E. Baldwin at the Wiston House conference, Frieder Roessler and Richard Blackhurst at the GATT Secretariat, and Dan Farber and Dan Gifford at the Minnesota Law School. I am indebted to each of them.

I owe a very special debt to the late Jan Tumlir, the former Director of Economic Research and Analysis of the GATT Secretariat. For almost a decade, Jan was a teacher, a friend and a model of what it means to have integrity in this business. His last words to me were about this study – a typically gruff complaint that I was avoiding several hard issues, coupled with an expression of his personal conviction that I would have something worthwhile to say about them. This study is dedicated to Jan's memory.

ROBERT E. HUDEC
Minneapolis
June 1987

DEVELOPING COUNTRIES IN THE GATT LEGAL SYSTEM

Contents

Introduction to the New Edition

J. Michael Finger

The history of GATT's relationship with developing countries began with what Robert E. Hudec describes as "a legal relationship based essentially on parity of obligation" {24}.[1] Yet as the GATT system evolved it increasingly left developing countries outside of the momentum towards liberalization that the negotiations built up among developed countries and exempted them from the general though imperfect sense of discipline that developed countries came to accept. From GATT's beginning through the mid-1980s – the period Hudec studied – the identity of developing countries in the system became almost entirely a matter of their demanding non-reciprocal and preferential treatment and developed countries responding grudgingly to those demands.

The result was a relationship that Hudec describes as "form without substance" {99}.

In form, the relationship was extensively elaborated:

> After years of debate and of gradual compromising, all the key ideas advanced by developing countries – non-reciprocity, preferences, special and differential treatment – were accepted at the formal level during the 1970s. They now appear in several GATT legal texts and in countless declarations. {155}

These expressions did not, however, have the force of international law obligation. The commitments were compromised by language such as "The developed countries shall to the fullest extent possible – that is, except where compelling reasons, which may include legal reasons, make it impossible, . . . "[2]

This is almost a mirror image of the "diplomat's jurisprudence" that Hudec in other investigations found to exist among developed countries.[3] This "diplomat's jurisprudence" was a compromise between jurisprudence as understood by lawyers and the reality of the limited influence trade negotiators had over national trade policy decisions. In an era in which there was sometimes a greater sense of shared objective among trade negotiators than

between these negotiators and government officials at home, not pinning down trade differences with legal precision could allow the working out of a mutually acceptable solution before the matter reached domestic politics.

If the system did not ask for reciprocity from developing countries in exchange for what they wanted, for example, better access to developed country markets, then how did it attempt to motivate developed countries to provide such concessions?

Hudec's answer: appeal to "the welfare obligation".

> The power to govern usually brings with it, according to most twentieth-century political norms, a duty to take care of the disadvantaged members of the group being governed. For example, it would not have been possible to create governing power in the European Community unless the Community undertook a responsibility to do something for the depressed areas within its domain. {31}[4]

Not reciprocity but rather the welfare obligation of the rich to assist the poor came increasingly to be the motive that the system called on to stimulate developed countries response to the demands of developing countries.

Hudec moves on to ask if further appeal to the welfare obligation – or to an alternative strategy in which developing countries' offered reciprocity – might be effective (a) to discipline developed country restrictions of particular relevance to developing country exports and (b) to support policies within developing countries that would help them to better use international trade as a vehicle for development.

As to influencing developed country liberalization, he concludes that the gradual pace of developed country liberalization is likely to continue but would not be significantly affected by either strategy. Likewise – writing in the mid-1980s – he saw neither strategy as likely to discipline the growing use of "voluntary" quantitative restrictions where developing countries were enjoying particular export success. The moral force of the welfare obligation had been spent and, so far as trade is concerned, refocused on the poor at home. As for reciprocity, developing countries did not have the economic size or power for it to provide them great leverage.

The one source of power the system might provide is the most-favored nation (MFN) principle:

> [T]he MFN obligation is, above all else, a legal substitute for economic power on behalf of smaller countries. {180}

But the MFN obligation, particularly with regard to developing countries, had been compromised. The institutionalization of special and differential

treatment for developing countries has been part of the general erosion of this principle.[5] What developing countries have gained from the granting of discriminatory treatment in their favor has been overwhelmed by this systemic erosion.

From this followed Hudec's first recommendation:

> [D]eveloping countries should re-direct their long-term objectives to the strengthening of the GATT's MFN obligation in all respects. {189}

His second recommendation was that:

> GATT's legal policy towards developing countries should change and . . . the Contracting Parties should instead establish a regime of developing country legal obligations that would provide support for governments of developing countries in opposing unwanted protectionist policies at home. {190}

"Unwanted protectionist policies" does not necessarily mean *all* protectionist policies. Hudec admitted the possibility that while some import restrictions will be wasteful, others could be constructive. Developing countries, like developed ones, would benefit from the support the system can provide to sort one from the other.

However, for the system to provide such support, developing countries would have to change their attitude towards it. Even on application and reform of GATT provisions such as Article XVIII's infant-industry protection provisions, the developing country stance had been simply to broaden what the provisions allow rather than to work for an effective differentiation of constructive from wasteful trade interventions. The system Hudec saw was about more latitude to intervene versus less, not about good intervention versus bad.

CONTENT OF THE INTRODUCTION

In the following parts of this introduction, I summarize the arguments behind these conclusions and recommendations – in a way that I hope will be a stimulus to read the book rather than a substitute for such a reading. I also report what I have learned from an examination of the citations the book has received in other published works.

The summary has been significantly influenced by what I learned from the citations. When I first read the book I interpreted it as a skilled example of what in my undergraduate days had been called "institutional economics" and has come since to be called "the new institutional economics".[6] However, I found