



*First Draft for Comments*

## **Towards a New Age in Special and Differential Treatment**

Javier Lopez Gonzalez<sup>1</sup>

Maximiliano Mendez Parra<sup>2</sup>

Peter Holmes<sup>3</sup>

May, 2011

### **Abstract**

In this paper we provide a historical and political overview of the origin and evolution in Special and Differential Treatment (SDT). We suggest that the current applicability of such treatment to the self-selecting 'developing country' grouping is no longer coherent given the huge heterogeneity of its component countries. We aim to provide a justification for a more targeted approach to SDT that is geared towards the development needs of the most vulnerable countries. To this end, we propose the use of observable criteria, serving the purpose of identifying capacity constraints, to determine selection into SDT provisions. We provide a discussion of a methodological framework that can be applied on an issue-by-issue basis and that relies on the use of composite indicators. These are aggregated using ranked criteria and take on a weighted structure and a set of thresholds that arise through a negotiated process. The secondary objective of this paper is to re-launch the debate on the reform of a system which has appeared to lose its development focus.

---

<sup>1</sup> University of Sussex & Iteas Consulting Ltd.

<sup>2</sup> University of Sussex & Iteas Consulting Ltd.

<sup>3</sup> University of Sussex

## 1. Introduction

Special and Differential Treatment (SDT) has been, either implicitly or explicitly, part of the international trading system since its birth after the end of World War II. The early days of the GATT bared witness to the recognition that developing countries could face difficulties in meeting the array of disciplines negotiated under the emerging system. This led to the notion of introducing flexibility measures, in terms of commitments and requirements, so as to achieve the integration of developing countries into the world trading system. Three broad forms of SDT can be identified; the first relates to market protection where developing countries are offered less onerous liberalisation schedules. The second is the extension of market access to developing countries where these receive preferential access into developed country markets through a waiver from MFN treatment under the 'enabling clause'. The third is a particular consideration to implementation issues where developing countries are offered derogations or special treatment on the basis of capacity constraints. These forms of SDT are a direct response to the increased involvement of developing countries in the world trading system and implicitly recognise sets of constraints that these countries face in their integration into this system. But whilst special derogations are extended to both Least Developed Countries (LDCs) and the self selecting developing country grouping, there is a growing consensus that the latter need be further differentiated on account of the growing heterogeneity between countries that compose this group.

In this paper, we seek to provide a review on how one would go about operationalising SDT so that it is made contingent on observable criteria that delimit the presence of a constraint which makes the extension of derogations desirable. This principle would then be amenable to *graduation* where countries that surmount these constraints would be re-integrated into the general commitments of the international trading system. We document the literature that supports a more targeted approach and suggest methodological steps that are needed for its operationalisation. In the process we argue that the constraints that countries face in meeting the growing demands of the international system can be subsumed into two broad categories. The first is domestic regulatory reform and the second is external market access. We identify sets of constraints that can be generalised for these two cases and then propose economic or analytical criteria that can serve identify the presence of these. We then discuss the use of such objective criteria and the possible methodologies that can be used in the creation of composite indicators.

The approach taken in this paper abstract somewhat from the normative aspects, and to a greater extent the negotiating realities of the international trading system. This liberty is not taken lightly but is necessary so as to provide a counterfactual world where SDT is granted on the basis of the actual

constraints that developing countries face. By freeing ourselves from the negotiating realities we can gain insight into the methodological constraints that arise in the operationalisation of such an idea. We discuss at length not only the links between identified constraints and the observable criteria that serve to capture these, but also the hurdles that one could face in combining a set of indicators so as to create lists of excluded countries. In the process we also document that hurdles that arise in delimiting graduating thresholds.

Our underlying assumption is that engaging in the international trading system is a beneficial endeavour; however it may come at a cost that a set of countries may be ill advised to pay given their current developmental situation. The Hong Kong Ministerial Declaration reaffirmed the importance of SDT in the international system but it is increasingly evident that the current time concessions on implementation provide little flexibilities for countries which are severely constrained. We push for a reform that ensures that the benefits of being treated differently reach those countries where the marginal contribution to development is the greatest and where free-riding can be minimised. To do this, we first need to identify the developing countries that are in a position to increase their commitments at the WTO given their level of development. Then we aim to identify those countries that can benefit from being treated differently due to their development process. We also consider that in the largest and more advanced developing countries there are still development issues that need tending to. There may be sectors or disciplines where some more advanced developing countries may still need further differentiation. This leads us to propose a system where the classification of countries, and hence participation in WTO modalities, is made on an issue by issue approach. According to each of these we identify a set of constraints that serve classify countries against each other. We then propose the use of these to negotiate a set of graduating criteria so as to identify who should or shouldn't implement any given WTO issue. In the process we show that there are many constraints that are common across WTO issues. For example, capacity constraints where WTO issues demand the incorporation of new legislation and control mechanism into domestic regulation can be identified through a particular set of indicators. Given that these capacity constraints are likely to affect various modalities in the WTO one composite indicator can serve across these. This classification of constraints provides an important step in the operationalisation of the principle of SDT which is the ultimate aim of the paper, it complements the analysis of Stevens (2002) and Cottier (2006) who attempt a similar task for Agriculture and Pharmaceutical patents under TRIPS respectively.

In the next section we present a short historical overview of the evolving nature of SDT. We focus on the underlying reasons that justify its application in view of identifying sets of constraints that countries face in their integration to the trading system. These will be implicitly and explicitly recognise throughout the negotiations process. In the third section we discuss how one can introduce more flexibility into current SDT practices in order to modulate participation in the system to make it contingent on developmental needs. The fourth section presents that methods that can be used in the creation of lists of excluded countries where we discuss at length the role of composite indicators. The final section concludes.

## 2. The Ages of Special and differential treatment

*New countries, development concerns and non-reciprocity*

The concept and discipline of Special and Differential Treatment (SDT), as established and regulated by the GATT and, eventually, by the WTO, does not appear until the Tokyo round in 1979; however, its main elements can be traced prior to this. More precisely, SDT has been steadily evolving since the creation of the GATT in 1947 where complete reciprocal commitments were the norm to an almost separate body of legislation.

Currently SDT principles are constructed on the basis of three main pillars: Market protection; market access; and Implementation concerns (Lichtenbaum, 2001). These three elements can be more deeply defined (Page, 2004) as:

- Market Protection: The permission to adopt policies contrary to the spirit of the WTO rules in order to reduce the cost imposed by the international trade system;
- Market Access: The granting of improved access to developed country markets in view of increasing the benefits of trade and;
- Implementation: The concession of delaying or partially fulfilling the obligations requested by others in order to reduce the potential associated costs of adapting to new trading conditions.

The path leading to the emergence of the above cited SDT elements is interesting as it provides a natural backdrop to the rise in the participation of developing countries in the world trading system. Additionally it hints at the possible constraints that these countries would face in the implementation of the growing disciplines of the system. As these , so too did the concerned voices of developing countries. Correspondingly the above outlined elements of SDT began to materialise. First appeared concessions on market protection; these were followed by preferential market access into developing country markets through the creation of the GSP; and then came transition periods offered in the implementation of Uruguay Round commitments. We present each element chronologically as it appears in the body of disciplines where we aim to identify the set of constraints that justified the extension of SDT so that we can attempt to capture these through the use of analytical criteria in subsequent sections.

The International Trade Organisation (ITO) did not materialise and, instead, a more modest and limited GATT was agreed. This agreement reflected the balance of power at the time and was shaped almost exclusively by the will of developed countries<sup>4</sup>. Only 11 out of 23 countries that signed the GATT in 1947 were what we now consider 'developing'. At the time, there was no official recognition

---

<sup>4</sup> With Europe and Japan completely destroyed and its recovery being almost completely financed by the US and the Soviet Union out of the agreement; it not entirely inaccurate to suggest that it was the United States who shaped the agreement.

of a developing country grouping<sup>5</sup>. As a consequence, very little special provisions for this type of country were foreseen and the agreement was almost entirely based on the principle of reciprocity and non-discrimination. The only exceptions granted were in the form of an authorisation, for the less advanced economies, to “deviate temporarily” from the provisions of the agreement according to article XVIII<sup>6</sup>. But the increased participation of developing countries in the international trade arena led to a wider recognition of the principle of SDT. The notion that countries at lower levels of development faced important constraints in meeting the growing demands of such a system became apparent. However in prescribing SDT provisions, the system predominantly relied on the base assumption that all developing countries faced the same set of constraints. Whilst there are certainly commonalities across developing countries, many asymmetries also emerged. This then cast a doubt on the suitability of a one-size fits all system of differential treatment.

### *Market Protection*

The idea that the current trade system could be in the best of the cases ineffective, and in the worse detrimental, in assisting development came to force. It was backed by the growing notion that terms of trade could act against development as first established by (Prebisch, 1950) and (Singer, 1950). They postulated that, in the long run, commodity prices would tend to decline relative to industrialised products driven by changes in world demand. This implied that developing countries had trade patterns that acted against their development needs. Moreover, given the volatility apparent in commodity prices, excessive reliance on exports of primary products could prove to be a ticking time bomb. As a consequence, the natural follow-through to this argument suggested that only through a process of industrialisation, which would change the underlying production structures, could development objectives be achieved. Developing countries needed, according to this view, to focus more on the gains from trade through domestic economies of scale rather than traditional comparative advantages given that these could turn their terms of trade against them. Whilst this hypothesis does not necessarily suggest that trade cannot be a development vehicle, it implies that developing countries, with non diversified production structures based predominantly on commodities, may suffer some drawbacks from the full participation in complete free trade.

These theories were the natural consequence of the academic and intellectual zeitgeist of the time, but the free market proponents were challenged by those that believed in more regulated or interventionist solutions. Prime examples of these challenges can be found in (Lipsey & Lancaster, 1957). They argued that interventionism could lead to second best solutions in the presence of distortions, giving important backing to theoretical justification for deviating from free trade practices. This last idea provided a justification to the incentives that already existed (and still exist) for counteracting others’ free trade with protectionist measures as underlined by (Scitovsky, 1941) and (Samuelson, 1962). Therefore, the early forms of SDT were granted on the basis of constraints that were due to the underlying economic activity of countries where particular attention was paid to the

---

<sup>5</sup> Brazil, Burma, Ceylon, Chile, China, Cuba, India, Lebanon, Pakistan, Rhodesia and Syria.

<sup>6</sup> Interestingly, we have now gone full circle where this is the system that currently governs SDT since the Uruguay round’s single undertaking.

type of products that were traded and the adverse effects that could be generated as a result. It gave backing to the notion that developing countries could engage in softer liberalisation to support industrialisation.

Industrial development would require protecting the expanding but still small domestic markets so that the necessary economies of scale could be attained and, eventually, competition with developed countries could be undertaken on an even keel. The rationale was then that new industries should be exempt from external competition during their conception. This would involve creating an internal trade diversion phenomenon where an implicit transfer of consumer surplus would be made to producers mediated by the higher domestic price that would have prevailed relative to free trade practices. This was the birth of the “infant industry” argument which suggested that industry protection was warranted, via higher tariffs or quantitative restrictions, to shield countries from more competitive imports so that an industrial base could be forged.

### *Market Access*

As the argument for protecting new industries gained momentum, so did the idea that developing countries should receive preferential access into developed country markets. This was more palatable in the wake of the independence that colonies were gaining at the time. Colonial provisions operated under the tenet of almost duty free access across colonial links. The change in this status also saw a change in the trading relations where preferences could no longer be extended as before. As a result, the second dimension of SDT emerged: Market access.

Lower tariffs for imports originating in developing countries would result in important changes in disciplines. Developing countries believed that the GATT was not properly addressing their trade concerns. This led to the creation of UNCTAD in 1964, which would deal with the trade and development agenda (Michalopoulos, 2000). In addition to playing a pivotal role in the establishment of a system of preferences, the creation of this organisation provided an important backing to the link between trade and development. It recognised that developing countries faced certain constraints in their integration to the international trading system. The first concrete measure in developing a system of preferences was made in 1965 with the addition of Part IV on trade and development to the GATT. Among other provisions, article XXXVI established that contracting parties should provide “more favourable and acceptable” market access conditions for products of developing countries. Moreover, it also stated that developing countries “should not be expected” to make concessions that were inconsistent with their development levels and strategies (Michalopoulos, 2000). There were also calls for the elimination of unreasonable differences in restrictions between primary and processed products. Finally, Article XXXVIII called for joint action, through international arrangements, to improve market access for products of export interest for developing countries.

Despite Part IV being hortatory in most parts or inscribed in what is considered “soft law” (Lichtenbaum, 2001) with an extensive use of “should” instead of “shall”; it made important points for developing countries concerns about trade and development. It addressed the issue of obtaining a more favourable or preferential access for their exports; it stated the principle of non-reciprocity in

concessions and furthermore it also addressed the issue of tariff escalation and peaks. Part IV and its articles would set an important foundation in the negotiations that would lead to the establishment of the Generalised System of Preferences (GSP) in 1968.

The GSP was effectively established in 1971 when a waiver for a ten-year period was granted to the MFN clause of GATT Article I. As a result developed countries began to implement their own GSP schemes with different scope but under the premise of non-reciprocity towards developing countries. The initial temporary waiver was finally made permanent when, in 1979, the “Enabling clause” (formally Differential and More Favorable Treatment, Reciprocity and Fuller Participation of Developing Countries) was included in the GATT.

The establishment of the GSP would have important effects on the multilateral trading system, not only through its trade effects, but also in terms of how disciplines and negotiations would be dealt with in the future. A major point of importance for developing countries was that the concept of non-reciprocity was made effectively binding. From this point onwards, developed countries would not expect full reciprocity in multilateral trade negotiations; as well as in bilateral negotiations even under Article XXIV<sup>7</sup>. However, in order to counterbalance the effects of non-reciprocity the “graduation clause” was introduced. By this clause, preferences could be removed as recipient countries reached a certain level of development. This graduation clause has been criticised on different grounds. On one side, it is argued that it may provide developing countries with wrong incentives towards further development (Tortora, 2003). This is because attaining competitiveness in a given sector would be met by the stick of removing preferences rather than an enticing carrot. On the other hand, it is argued that preference granting countries, being the ones who decided the criteria and disciplines for graduation, would leave developing countries vulnerable to extortion. This particularly for obtaining additional commitments given a possible loss in bargaining power (Whalley, *Special and Differential Treatment in the Millennium Round*, 1999). The “discretionary” application of graduation according to criteria set-up by the ‘donors’; as well as the power to regulate the scope and the coverage could be considered as ill suited to the particular development needs of countries. However the principle of graduation itself provided an interesting recognition of the dynamic adaptation of countries to changing world conditions. These graduating criteria were generally delimited through observable indicators that related to market shares in donor countries. An implicit threshold would be set and countries breaching this would be exempt from preferences. But these were criticised on two grounds, first the preferences were non-binding as above stated, but second, the graduating criteria or threshold were devoid of objectivity. This second point identifies a major hurdle in our application of graduation to SDT. To the extent that a line need be drawn to determine participation in the GSP, the same will apply for SDT. But this may be a negotiating issue that can be surmounted and will be discussed at greater lengths in subsequent sections.

Another interesting implication of the “Enabling Clause” as well as Part IV of the GATT was the appearance of the Least Developed Country (LDC) grouping as a subset of the developing country

---

<sup>7</sup> As seen in the ‘substantially all trade’ wording of this article



group. This was the first identification of a grouping under the GATT. It provided the first precedent to a differential treatment towards countries in particular developmental situations. This remains the only clearly defined grouping in the context of the GATT. It is based on a low income per capita in conjunction with varying other indicators (moderated by the United Nations). But the “developing country” category was, and continues being, a self selecting label. However, on the back of this first differentiation that implicitly recognised particular development constraints, one can call for further differentiation. The different development paths across the developing country grouping may warrant this. The Latin-American and African experience of “Structuralism” as contrasted with growth, structural adjustment and, eventually, industrialisation achieved in South East Asia portrays very distinct development paths. These may in turn also serve to support further differentiation of commitments.

#### *The Uruguay Round and the single undertaking*

The Uruguay Round (UR), launched in 1986 and concluded in 1994, was a very ambitious negotiation round both in terms of depth and range of issues. Developing countries would play a key role during its negotiations and the different characteristics and development paths of the negotiating developing countries would begin to become more apparent and translate into varying demands for differential treatment.

The *a la carte* participation (Hoekman & Ozden, 2005) in the preceding trade rounds where implementation was on a voluntary basis was to be no more. This resulted in developing countries needing to play a more active role in the design of commitments of the different modalities of the trading system. The introduction of a *single undertaking* would mean that developing countries would become subject to most commitments and disciplines that the agreement would produce. This would have important effects on both the negotiating process and the SDT provisions implicit in the new agreement. The wider participation and involvement of developing countries in the design of the disciplines would contribute to a change in the balance of power in the decision making process of the GATT. It would also underline the need for derogations from agreed principles for countries which faced particularly onerous costs in implementing all the agreed provisions. (Page, 2004) argues that the UR was the first instance in which developing countries were in a position to voice their concerns.

The single undertaking, by not allowing members to cherry-pick the disciplines they wanted to adhere to, altered the earlier established non-reciprocity For developing countries. Additional transitional periods of time to adjust to the disciplines that would emanate from the round were granted. This would then give rise to the third element of SDT where countries would be given enhanced policy space for transition purposes.

#### *Implementation of enhanced commitments*

Implementation concerns arose as a result of the acceptance of the presence of technical difficulties faced by developing countries in implementing commitments that went beyond the removal of traditional barriers to trade. It was understood that the implementation of the disciplines negotiated during the UR would require substantial technical capacity, one that was lacking in many developing countries. As a result, longer implementation periods were granted so that developing countries could adapt to incorporate new negotiated disciplines. But many developing countries, voiced the concern that longer implementation periods fell short of developing country needs. They called for increased technical assistance commitments for the implementation of the new modalities. These were included in the agreements but appeared as non-binding ‘best-endeavour’ clauses which could be ineffective in delivering the desired development objectives (Lichtenbaum, 2001). However, their inclusion would have important implications in the future SDT.

The UR revealed diverging interests within the developing country grouping. This was reflected through the appearance of negotiating groups with diametrically opposed interest. Whereas the interests of developing countries in earlier rounds had been seen as homogenous across developing countries, the emergence of new negotiating groups cast a shadow on this concept which could no longer be ignored. One of the sources of this new found heterogeneity across developing country priorities arose from the different developmental experiences<sup>8</sup>. A second factor giving rise to varying positions across the developing country group would be attributed to the different composition of traded products across the developing country grouping and in particular the introduction of the new Agreement on Agriculture (AoA). Until the UR, agriculture had mostly remained outside the disciplines of the GATT<sup>9</sup> but its introduction blurred the distinctions between and within developed and developing countries. Common positions were found between developing exporters of food such as Argentina, Brazil or Malaysia with some developed country producers and exporters of food the likes of Australia, Canada and New Zealand. But the Cairns group position for undistorted free trade in agriculture would be opposed by many developing countries who were willing to sideline with the EU, US and Japan for a more restricted treatment of agricultural trade. The fracture in the once common developing country position on certain negotiating issues underlined the growing heterogeneity across this self-selecting group. To the extent that these differing positions would transpire from diverging constraints or interests they would provide some backing to the case of further differentiation across countries.

The introduction of the single undertaking played an important role in generating these divisions. Where the prior *a la carte* approach implied that countries were free to cherry pick their participation into the varying agreements, the introduction of the single undertaking required consensus building. The *variable geometry* that preceded the UR facilitated like minded countries to reach accord on similar minded issues. The introduction of the single undertaking required that accord be reached by

---

<sup>8</sup> It would relate to the historical use of import-substituting policies across different regions. Whilst South-east Asia was more inclined to market liberalisation, Africa and, particularly Latin America, had developed strong internal lobbies that pressured governments to maintain protectionist measures.

<sup>9</sup> This is because agriculture was, and to this day remains, one of the most complicated and thorny issues in international trade negotiations.

all countries, like minded or not. This resulted in an important fracture in consensus building across the now patent, and sometimes completely polarised, interest of countries.

The elements above presented; different experiences in development; a stronger position of developing countries; and the divergence in the developing countries position, had important effects on the disciplines and characteristics of SDT. As way of example, the introduction of the AoA gave rise to new justifications for SDT on the basis that trade liberalisation could cause damage to food security. Additionally growing concerns on the special role of agriculture in development were voiced (Matthews, 2007). Therefore, SDT after the completion of the UR in 1994 reflected the existing differences within the developing country grouping but also paid heed to other growing development concerns of these countries.

#### *The Doha Round and further differentiation*

Developing countries felt short-changed from the outcomes of the UR, but on a positive note it seemed to give them a new found impetus, through the recognition of a stronger negotiating position in the international trade arena, for a more favourable agreement. This new found negotiating force allowed them to effectively block developed country intentions in Singapore where the introduction of new disciplines in trade related issues, the so-called Singapore Issues, were being negotiated. In addition they spurred a forestalling of the negotiations in Seattle in 1999 by refusing to accept a process in which they were effectively being excluded (Page, 2004). There would not be another Blair House Agreement, developing countries had found their voice.

By the end of 2001, the Doha Round is launched. It is baptised as the Doha Development Round, manifesting the aspirations of developing countries. This round was set to fix the perceived developmental mistakes made in the UR. Its emphasis on development would try to attend to the varying needs of developing countries by defining the channels through which trade could best serve their development needs. The early results, where SDT is concerned, were promising with the achievement of differential treatment forming 'an integral part' of the WTO in the Honk Kong Ministerial. But the idea that "one size does not fit all" (Matthews, 2007) began to emerge. A greater differentiation across countries could help improve the efficiency of current SDT provisions by aiding in the targeting of such policies.

A salient issue though is that, under the market access umbrella, the benefits of differentiation and special treatment are becoming smaller. As developed countries (and developing countries as well) reduce their tariffs through participation in bilateral agreements, the marginal utility of preferences falls through the fact that more countries have access to these. Moreover, further MFN liberalisation also erodes preferences by eating away at the preferential margins hence diminishing the benefits of SDT in market access. As a consequence, the reaction is trying to increase the disciplines under SDT and also, if possible, trying to differentiate from the rest of the developing countries.

With respect to the implementation dimension of SDT, for the first time, recognition is given to the fact that, that besides additional time and capability building, developing countries need financial

resources to aid them in complying with WTO disciplines. This implicitly recognises the impact of the adjustment process as well as the need to develop infrastructure and other capabilities to effectively extract the maximum advantages from trade liberalisation. Developing countries were demanding additional aid to tackle with their supply and institutional constraints but also, and more controversial, the adjustment costs that trade liberalisation may put upon them (Cernat & Mendez Parra, 2008). This suggests that developing countries see trade as an important tool for development but not a sufficient condition for it. In consequence, they look for assistance in dealing with both the costs and the losers that arise via trade reform. Despite not being included as an SDT discipline in the HK declaration, Aid for trade aims to address all these problems more directly than the standard SDT disciplines which may warrant further analysis.

The Doha Round is still under negotiation as these words are written. Compared to the UR, this round includes both more negotiated disciplines and negotiating parties. In fact, China is now a key member that was not part of the UR. Therefore, a longer and more complex negotiating period should surprise no one. However, even more challenges have arisen after the failures in negotiating the 'Singapore issues' and the proliferation of bilateral agreements. These issues have led to a wider discussion on the challenges to a single undertaking. The discussion is about the fundamental debate about the depth and the width of the agreements. Should the system make few demands reaching every member or should members progressively adopt deeper commitments? Moreover, particular complications arise as a result of the different modes of integration of domestic and the international law and/or the different division of power between federal and national legislatures across members. (VanGrasstek & Sauve, 2006) As a consequence, the single undertaking leads, as we have seen, to the constant creation of exceptions to the main rules and lead to the necessity for applying SDT provisions.

An alternative to this would be to move to, or return, to a system of *variable geometry*. This approach was supported by the European Union during the negotiations of the 'Singapore issues' where a plurilateral approach to negotiations would emerge with separate negotiating parties based on the desired adoption of these measures. The principles behind variable geometry have already been applied in the wider integrating efforts of the European Union as evidenced through the single currency and the Schengen Agreement (Cottier, 2006). However, as in the European Union, some disciplines must be adopted by all members and the proposal made by the EU only applied this principle to 'new' issues in negotiations in order to achieve a 'Doha plus' agreement.

However, the wider, and perhaps more important question is that treating the exclusion of countries from disciplines and the avoidance of free-riding so as to appropriately share the burdens of liberalisation. In the case of the 'Singapore issues' this was only a problem with investment, however, it may be an issue in other future topics. Nevertheless, the effects of a variable geometry approach to negotiating issues goes beyond the current negotiating concerns and delve deeper into the core of the decision making process of the WTO (VanGrasstek & Sauve, 2006). It is clear that the single undertaking and the norm of consensus are two of the key reasons for the deadlock in negotiations and the lack of progress.

However, it seems that the pledge to return to the *a la carte* approach is based on some kind of rebalancing of the efforts of liberalisation between developed and developing countries. Hoekma et al (2003) call for the creation of ‘policy space’ in this respect. But until then, a further examination into the rules for graduation, the need for further ‘means-tested’ differentiation is warranted. This SDT may help smoothen the negotiation process at the WTO.

### **3. Towards a change in Special and Differential Treatment**

Making Special and Differential Treatment “an integral part of the WTO” (Hong Kong Ministerial declaration) is likely to require a re-evaluation of the current approach if it is to move from an adjustment tool to a development one. This is because, as it currently stands, best-endeavour clauses and time concessions granted provide developing countries with a non-binding and depreciating flexibility asset which has often been said to be ill suited to the desired development objectives<sup>10</sup>. This last point is made implicit in the continuation of the above declaration where a call for a review of current practices, in view of strengthening the system and making it “more precise, effective and operational”, is put forward. In this section, we shy away from the broader discussion on the merits and pitfalls of SDT so that we can focus on the question *for whom and how?*<sup>11</sup> We aim to look at the consequences of developing a more unified SDT selection procedure that hinges on the creation of an outcome based system where opt-outs or graduation is made contingent upon a set of analytical criteria. This ‘means-tested’ approach to SDT is not new. A practical implementation of it can be found in Stevens (2002) for the case of the AoA. In addition, the underlying principles are also present in the EU’s GSP scheme where trade based criteria determine the type of preferential market access granted into the EU<sup>12</sup>. The contributions of (Hoekman, Michalopoulos, & Winters, 2003), (Kleck & Low, 2004), (Cottier, 2006) and Chang (2007) also lend support to the use of such criteria based approach for determining SDT. We draw on this literature to provide a practical implementation to this approach. We pay particular heed to the needed assumptions, possible consequences and implementation shortcomings that could arise from its operationalisation.

The implicit use of objective criteria determining the status of LDCs, and hence exemptions to particular WTO provisions, sets an important precedent to our story. If one can identify the most vulnerable economies on the basis of objective criteria, then it follows that one should be able to

---

<sup>10</sup> See (Kessie, 2000) for a discussion on the enforceability of SDT provisions under the WTO. The notion of a depreciating asset is from (Stevens, 2002) and alludes to the value of SDT that declines with the ticking of time. Also see (Page & Kleen, 2005) for a discussion on SDT and development outcomes.

<sup>11</sup> For a comprehensive review of SDT and development needs readers are pointed to the extensive coverage of these issues in (Page & Kleen, 2005), (Kleck & Low, 2004) and (Hoekman, Michalopoulos, & Winters, 2003)

<sup>12</sup> Countries can only access the GSP+ scheme if their total share of world trade does not exceed 1%. Countries can also graduate away from GSP preferences on a sectoral basis when their market shares reach a certain threshold. Although strictly speaking this application of GSP practices is not regulated under WTO legislation, its application is a good example of how analytical criteria can determine the application of differential treatment in market access issues.

explore the use of a similar technique for further differentiation. This is desirable because the current application of SDT provisions is reserved to a self-selecting 'development' group and hence not commensurate on the actual degree of economic development. It places more industrialised economies (China, Brazil, Mexico or Korea to name but a few) in equal footing, in terms of commitments under the WTO, with countries which may be much less developed (such as Cameroon, Nigeria or Kenya). Where this heterogeneity across countries within the 'development' group may reflect an underlying heterogeneity in the capacity and indeed desirability of implementing more complex WTO commitments, there may be a case for a more targeted form of differentiation for SDT purposes.

The implicit assumption that permeates throughout the remainder of this paper is that there is sufficient momentum behind the idea that participation in more complex WTO provisions should be made contingent upon levels of development<sup>13</sup>. Using this assumption releases us from two important debating issues. The first is that of the legality and practicality of changing the current group classification under the WTO where differentiation across the self-selecting development grouping is 'means tested' on the basis of differing criteria. The second is that of allowing us to abstract from the broader discussion on the actual benefits of applying SDT provisions. There is a wide debate on this last issue that relates to the benefits of binding policy where delays in doing so can bring short term gains but have longer term consequences. A wider issue is that there remains an important bias towards protecting one's economy from international competition. Irrespective of the reasons for this bias, one has to keep in mind that there is a strong economic argument in favour of reducing cross-country barriers to trade. This would both facilitate the efficient distribution of production and also enhance competition by providing a more level playing field. Any SDT provisions will have to be weighed against these goals. Both on how these are affected in the short and long term, and on how countries will tend towards protectionist measures. Following these assumptions allows us to focus on the operationalisation of SDT rather than its justification.

### **A means tested approach to SDT using analytical criteria...**

The use of an analytical criteria based approach determining participation in SDT provisions facilitates a more flexible and targeted modulation of SDT commitments. One where participation is made contingent on the specific needs of countries concerned. The main justification for the use of such opt-out provisions is the understanding that some countries may be ill-equipped (due to a lack in institutional capacity; supply side constraints; or other developmental needs) or ill-advised to implement some WTO provisions. This implicitly recognises that, whilst there are important benefits to liberalisation, there are also large associated costs, and both of these are asymmetric across countries. As way of example, the transposition and implementation of commitments under the

---

<sup>13</sup> This issue is a contentious one because international trade theory suggests that the majority of gains from international trade are derived from domestic liberalisation. Postponing reform could be tantamount to postponing these benefits.

TRIPs agreement is likely to provide a level playing field for all parties concerned. However this is likely to be most beneficial to countries heavily engaged in IP intensive trade. Those that are not will stand to gain little and are also likely to impose smaller negative externalities on those that are. In addition the costs of implementation will also vary widely. This is not only due to a strong variance in the institutional capacity of countries across levels of development, but also to the presence of higher opportunity costs. The implementation of such commitments may come at the expense of other more pressing development necessities (Page & Kleen, 2005). This suggests that, if SDT is to take a development role, exemptions from WTO provisions should be made on the basis of the varying needs of developing countries. This point is first made by (Wang & Winters, 2000) who argue for higher flexibility in the application of rules; longer transitional periods; and technical assistance to support transition. If specific needs and constraints of developing countries can be captured by way of analytical criteria then the use of these in determining SDT status should be explored.

Proponents of changes in SDT provisions tend to share the common belief that analytical criteria should play an increasing role. These can be applied on an agreement-by-agreement basis (Stevens, 2002) and (Cottier, 2006), or alternatively by way of a more narrowly defined classification of countries such as an “LDC+” grouping as proposed by (Hoeckman, Michalopoulos, & Winters, 2003)<sup>14</sup>. The latter are also favourable to the creation of “*country-based criteria that are applied on an agreement-by-agreement basis to determine whether (when) agreements should be implemented*”. Irrespective of the outcome, this approach also lends itself to the introduction of a set of graduation constraints (Cottier, 2006). These can ensure that country exemptions from WTO provisions are only so until there is sufficient evidence of change from the initial pre-conditions that identified these countries as vulnerable. It introduces a more flexible and less arbitrary approach to SDT than the current practice of awarding fixed time constrained transition periods. Once the use of such an approach has been accepted, the challenge becomes one of “defining [the] analytical criteria that are relevant to specific SDT treatment concerns” and measuring these with existing data (Kleck & Low, 2004). It is in the exploration of this issue that we concern ourselves presently.

(Stevens, 2002) was first in developing an analytical criteria based approach for the application of SDT provisions. He did so for a “worked example” looking at the possibility of applying differential treatment, under the AoA, to countries that suffer from food insecurity. In doing so he sets up a methodological procedure that can be used as a baseline approach to other agreement by agreement SDT applications. First, one needs to identify whether a “one-size-fits-all” policy is adequate under a particular WTO agreement. Or, in other words, if there is a justifiable case for the application of differential treatment for a given issue. Where there is, then one can move to the second step which requires identifying the countries that should benefit from such treatment based on the desired objectives. Here Stevens proposes grouping countries on the basis of shared similarities amongst themselves but dissimilarities with respect to other countries. This requires identifying a set of criteria that make certain countries ‘different’ from the rest, but sufficiently similar to each other to warrant

---

<sup>14</sup> See also (International Food & Agriculture Trade Policy Council, 2004) and (Matthews, 2007)

the same type of differential treatment. The third step then involves the ‘modulation’ of commitments where the extent of the SDT is determined.

The scope for learning important procedural lessons from (Stevens, 2002) motivates a finer review of his methodology. Stevens begins with the identification of a justification for applying SDT under the AoA agreement. He argues that countries that are ‘food insecure’ could be exempt from onerous AoA provisions, but countries may fall under this category in two instances. The first is where agriculture plays a significant role in the economy and there are concerns of shortfalls in national production capacity. The use of subsidies to create price incentives that boost production may then be justified. The second is where countries have weak trade entitlements and may suffer from a lack of access to food imports in the future. To differentiate across these countries, Stevens proposes the use of a set of analytical criteria. The key starting point is the ex-ante identification of the reasons under which SDT should be granted. This should be tailored to the varying needs of countries within the similar food insecure category. Here echo is made to (Kleck & Low, 2004) statement that “the core challenge is to link negotiating positions on liberalisation commitments, WTO rules, and special and differential treatment to a clear and cogently argued identification of development needs and priorities”. The needs-based approach then paves the way for the modulation of SDT commitments. Where the outcomes identified are different, they will require the use of different identification criteria.

Stevens proposes a high share of agriculture in GDP but a low share of per capita calorie supply to categorise countries falling within the first group. For the second he argues that high food imports as a share of GDP; high degrees of vulnerability; and low per capita calorie supply can be used. The combination of these indicators should then allow us to inform the choice of the groupings that should receive SDT under the AoA. Stevens compares the largely self-selecting NFIDC grouping to one serving a similar purpose but that is identified using his selected analytical criteria<sup>15</sup>. He first examines the country overlap between the NFIDC group and one selected on the basis of a minimum calorie supply. This benchmark criteria is an annual average variation corrected nutritional minimum (from WHO recommendations). Stevens’ initial findings suggest a large variance in the countries that can be identified as ‘food insecure’. With a cut-off point of 2500 Kcals of supply per person per day, 25 countries that do not belong to either the LDC or the NFIDC groupings appear to be ‘food insecure’. In addition there are several LDCs and NFIDCs that show a calorie supply above the chosen threshold and hence may not necessarily be ‘food insecure’<sup>16</sup>. This first attempt at the use of analytical criteria is perceptive in that it clearly exposes some of the shortcomings in the self-selecting nature of some groupings, this despite only being based on one indicator. Stevens then combines this indicator with one looking at agriculture value added as a share of GDP to further refine the identification of countries which may be entitled to SDT. Here, similar results emerge. There are important

---

<sup>15</sup> The NFIDC group is based on three criteria. A country has to have self-selected as developing, it must notify the WTO that it wishes to qualify as an NFIDC and it must be a net importer of certain foodstuffs during any of three years where data is available.

<sup>16</sup> Although these are largely NFIDCs (11 countries) where there are two LDCs that show a calorie supply above the chosen threshold.



discrepancies between the countries selected using the criteria and those that currently belong to the NFIDC grouping.

Some observations need be noted from this exercise. One points to the fact that neither approach (self selection or objective criteria based selection) provides a benchmark of who *should* be exempted. Hence there is no yardstick to which one can calibrate the criteria. If one holds true the principle that *no* country with a calorific supply above the chosen threshold can be deemed as food insecure, then there is evidence supporting the imperfect composition of the NFIDC grouping. However, if there are other factors that determine food insecurity that cannot be measured, then we need approach the issue with caution. In addition one needs to make judgement on how countries that fall between criteria are to be treated. If one country has a daily calorie supply above the threshold but then falls within the range of the other indicators, is it to be excluded on the basis that it does not satisfy both criteria? Or alternatively, is it to be included because it satisfies at least one of the criteria? These questions allude to the greater problem that is posed on how to combine the different criteria which we turn to in a subsequent section.

(Cottier, 2006) provides another example where scheduling of commitments could be investigated. He argues that developing countries may be capacity constrained in their implementation of patenting provisions for pharmaceutical products under the TRIPS agreement. Where there is support to the notion that a 'one-size-fits-all' policy may be ill-suited, he calls for an approach where graduation into a scheduled implementation of commitments is triggered. Countries then "introduce patent protection for a particular sector once their domestic industry has achieved a defined level of competitiveness in accordance with a threshold defined on economic factors and data" (Cottier 2006:p.38). Precedent to this type of SDT approach can be found in the Agreement on Safeguards where art. 9.1 footnote 2 exempts the application of safeguards on developing countries if the share of imports from these is below a given threshold. It then seems implicit that after this threshold is breached, the application of safeguard measures on developing countries is justified. In a similar guise, Cottier argues that provisions relating to the patenting of pharmaceuticals should only be introduced as countries reach competitive maturity. As in (Stevens, 2002), the issue then becomes one of identifying how developing countries are constrained in their application of WTO provisions, and then how economic indicators can serve the purpose of identifying these constraints.

A natural starting point to this exercise would be that of using simple revealed comparative advantage (RCA<sup>17</sup>) indicators calculated on pharmaceutical products and serving the purpose of identifying a country's competitiveness. But relying solely on this indicator does not necessarily capture the desirability of extending SDT provisions to a country. One also has to take into account levels of development; health outcomes; and the extent to which such SDT provisions could negatively impact

---

<sup>17</sup> Balassa (1968)

third countries<sup>18</sup>. Starting from the last criteria, countries occupying lower shares of world GDP are likely to induce smaller negative externalities on third countries through the non-implementation of a WTO provision. Turning then to 'health security' issues, it can be argued that countries which are most vulnerable should be exempt from onerous provisions. Here health indicators such as death rates; prevalence of disease; or life expectancy can be proposed. Dealing then with levels of development one can argue that poverty headcounts; GDP per capita; and net ODA (overseas development assistance) received as a share of GNI or per capita can serve the purpose of identifying countries that are most constrained in their development process.

Both (Stevens, 2002) and (Cottier, 2006) analyse SDT under a domestic regulatory perspective. In both instances, implementation of WTO provisions into domestic regulation is challenged on the basis of domestic constraints. However, there is another instance where countries may be entitled to SDT which relates to the preferential access to external markets. These are *enabling clause* provisions that give rise to the GSP and do not demand domestic regulatory reform. They deal with providing developing countries with preferential market access as a means to promoting integration into the multilateral trading system. We abstract from the justifications, or indeed the benefits, of these provisions as these issues are beyond the scope of our present focus, instead we look at how these preferences are operationalised<sup>19</sup>. The GSP allows for derogations from the MFN principle in the application of tariffs to developing countries. In the EU three separate regimes that differentiate across developing countries exist under this umbrella; the GSP; the GSP+; and the Everything But Arms (EBA). The GSP offers tariff preferences to all developing countries where duty-free market access is given to a proportion of goods and preference margins of 3.5 percentage points are given in products that are deemed 'sensitive'. The GSP+ then offers additional preferences to a select group of developing countries that are considered vulnerable or are in the process of implementing a set of internationally recognised agreements. The EBA grants near duty free market access to LDCs. It is in the criteria used to differentiate between these groupings that we are concerned with as procedural lessons that can apply to a generalisation of SDT practice can be learned.

In particular the differentiation across developing countries is of interest as it is closely related to the goals of this paper. There is a clear distinction, under the WTO, between treatment of LDCs and that of developing countries. In allowing for a differentiation across developing countries, the EU may have set precedent to such practices which could be extended to other WTO provisions. Here focus is on the developments that led to the creation of the GSP+ grouping. It was through a WTO dispute that the EU was required to aggregate its earlier enabling clause regimes into the GSP+. It was argued that differentiation across developing countries was counter to WTO provisions. The ruling of the dispute settlement procedure concluded that differentiation across non-LDCs countries could be made provided it was on the basis of "a widely-recognized development, financial, [or] trade need."

---

<sup>18</sup> Whilst a measure exempting the implementation of patents on pharmaceuticals has a clear impact on internal and external competitors, it also has wider implications for any and possibly all external competitors. These should be inversely proportional to the size of the market where the exemptions have been granted.

<sup>19</sup> See (CARIS, 2010) for a wider discussion on the benefits of the EU's GSP scheme

(CARIS, 2010). Taking heed of this then motivated the selection of GSP+ countries by way of varying analytical criteria. Countries would be eligible for the GSP+ preferences provided; they have developing country status; the five largest sections of GSP covered exports to the EU account for over 75% of total GSP covered exports; and GSP covered exports represent less than 1% of total GSP imports. Despite the application of the general GSP schemes not being under the purview of the WTO, the WTO ruling, and the subsequent action taken, provides an important nod to the use of analytical criteria for determining participation in SDT provisions<sup>20</sup>. These are clearly based on the principle of a country's export vulnerability and implicitly competitiveness in a given market.

Another salient feature of the EU's GSP scheme is the provision of a graduation clause. On the basis of certain trade based analytical criteria, developing countries can graduate out of the favourable preferences granted. The implicit assumption is that as countries become competitive in their exports of a given product category, the justification for granting differential treatment no longer holds. Countries then revert back to facing MFN tariffs for the products where competitive maturity has been achieved. Under the EU's GSP scheme, graduation is triggered (or competitive maturity is reached) when a country's exports in a given product category exceeds 15% of the EU's imports from all other GSP countries in that category of goods<sup>21</sup>.

The use of such competitive measures to differentiate across countries and sectors provides a targeted, or means tested, form of SDT which is commensurate on particular country characteristics. The EU GSP case serves as a good example on the use of analytical criteria and the modulation of SDT provisions. These being made contingent on both country characteristics and measures of competitiveness across sectors. In the following section we draw on the various lessons derived from the literature to provide a case for a more systematic approach to SDT.

#### *A more systematic approach*

To operationalise the concept of SDT a differentiation into two distinct modalities is required. The first pertains to differential treatment with respect to commitments of domestic regulation as per the different WTO agreements. This we call *domestic regulatory reform* and cite the above exposed examples in (Stevens, 2002) and (Cottier, 2006) as interesting case studies. The second then relates to differential treatment in market access to external markets. This we refer to as *external market access* issues for which the EU GSP scheme is a good example. It then follows that internal constraints in the application of SDT provisions are going to differ from issues that have to do with external market access. The former will require a wider investigation on the reasons that drive the internal constraints whereas the latter should hinge on the competitive nature of the countries or sectors concerned.

---

<sup>20</sup> The case against Pakistan qualifying for the GSP+ scheme brought forward by India due to the latter not satisfying the 1% criteria lends further support to the acceptance of such practices.

<sup>21</sup> This condition has to hold for the least three consecutive years. In addition, the threshold is of 12.5% for products under the Textile and Clothing sector.

## *Domestic Regulatory Reform*

First, we turn to finding if there exist a certain set of commonalities that can justify the application of SDT provisions based on domestic regulatory reform. For example, there is support to the notion that lack of institutional capacity can serve as a justification for differential treatment to be applied in more onerous WTO provisions. If institutional capacity, or more precisely a lack thereof, can be identified through a set of indicators, then one can use this as an arbiter for the modulation of certain WTO commitments. This indication of institutional capacity constraint can then be applied under an array of WTO provisions where the key constraint for implementation is the lack of capacity (e.g. TRIPS, GPA and Competition policy). One can propose indicators such as; per capita receipts of ODA; per capita tariff revenue; or per capita government expenditure as appropriate identifiers of capacity constrained countries. Similarly, one can think of indicators that measure the extent to which non-participation in a WTO agreement can affect third parties. This could be measured, as already proposed, through the use of country GDP in total world GDP or similarly through the share of trade of a country in world trade. Hence one can tie the indicator based approach to particular country 'conditions'. This approach is similar to that of (Stevens, 2002) where the 'condition' that justified the application of SDT in the AoA was food insecurity. It then becomes relevant to identify conditions which may constrain certain countries in their application of WTO agreements. Some of these can be overarching whereas others may only be relevant to a particular issue. Of the former, we believe that the impact on third countries condition should hold an important regard in any application of SDT. Hence, if a country has a large market, then considerations on the negative impact on third countries derived from benefiting from SDT treatment should generally be accounted for. In Table 1 we identify a set of conditions or constraints that can justify, or trigger, the application of differential treatment. We aim for a pre identification of sets of constraints as delimited in the literature. These are not linked to specific WTO agreements and also do not discuss the modulation of the required differential treatment, however they identify particular weaknesses that may call for differential treatment. These conditions can then be defined via a set of proposed indicators which can be retrieved from internationally available datasets. It follows that special provisions would be contingent on thresholds that identify when countries fall within the set of conditions. The first row of the table provides a summary of the indicators that Stevens (2002) uses to identify countries that may fall under the food insecure category. It is related to the domestic regulatory reform category because it may require the use of some domestic policies that can serve overturn the condition. The second row then tries to identify the indicators that would serve to capture institutional capacity constraints. As with the food security category, countries falling under this condition may be ill equipped to adapt domestic legislation to international standards. Note how this does not discuss the benefits that may be derived from doing so, just the idea that transitional periods of implementation, such as those that are now present, would be contingent on surmounting this condition and limited not in time, but rather in accomplishments of surpassing the minimum standards set via a threshold. One can think of the requirements of the TRIPs agreement as an example where institutional capacity constraints may play a role in determining the desirability of countries receiving differential treatment. Health insecurity then would serve the purpose of identifying countries which may be exempt from particular

provisions on the basis of particular endemic health outcomes. One may wish to be less strict in the application of TRIPs commitments for pharmaceutical patents in these countries to facilitate access to much needed medicines.

**Table 1: Symptom Checker**

<b>Condition</b>	<b>Symptoms (indicators that capture condition)</b>
Food insecurity (Stevens, 2002)	<ul style="list-style-type: none"> <li>- Calorie supply per person per day (FAO)</li> <li>- Agriculture exports as share of GDP (WDI)</li> <li>- Agriculture exports as share of world Agriculture exports (COMTRADE)</li> <li>- Composite vulnerability index (from Commonwealth secretariat 1999)</li> </ul>
Institutional capacity constraints	<ul style="list-style-type: none"> <li>- Per capita government revenue (can also be proxied by per capita tariff revenue) (WDI)</li> <li>- Receipt of ODA as share of GDP (WDI)</li> <li>- Per capita employment of government officials (?)</li> <li>-</li> </ul>
Health insecurity	<ul style="list-style-type: none"> <li>- Death rates ((WHO)</li> <li>- Prevalence of disease (WHO)</li> <li>- Sanitation (WHO)</li> <li>- Life expectancy (WHO)</li> </ul>
Negative impacts on third countries	<ul style="list-style-type: none"> <li>- Share of GDP in world GDP (Penn World Tables)</li> <li>- Share of trade in world trade (COMTRADE)</li> </ul>
Reduced productive capacity	<ul style="list-style-type: none"> <li>- Herfindhal indicator on export concentration (COMTRADE)</li> <li>- Herfindhal indicator on import concentration (COMTRADE)</li> </ul>
Opportunity cost variables	<ul style="list-style-type: none"> <li>- Health insecurity (see above)</li> <li>- Food insecurity (see above)</li> <li>- Education deficiencies (WDI)</li> <li>- Infrastructure variables (paved roads) (WDI)</li> </ul>
Poverty	<ul style="list-style-type: none"> <li>- Poverty headcount (WDI, World Bank)</li> <li>- Poverty gap (WDI, World Bank)</li> </ul>
Infrastructure deficiencies	<ul style="list-style-type: none"> <li>- Paved roads km (WDI)</li> <li>- Port facilities (WDI)</li> <li>- Landlocked status (CEPII)</li> </ul>
Political instability	<ul style="list-style-type: none"> <li>- Presence of conflicts, civil wars etc</li> </ul>
Specific conditions	Here the above would need to be complemented with issue specific indicators. Hence if we are treating
Competitiveness (sector or product specific)	<ul style="list-style-type: none"> <li>- Revealed Comparative Advantage (COMTRADE)</li> <li>- World market shares (COMTRADE)</li> <li>- Market shares in a given country (COMTRADE)</li> </ul>

The primary advantage of this approach is that it directly identifies the development needs or constraints of a given country. It is on the basis of these that any differential treatment should be

justified. Such a method implicitly introduces the concept of graduation where a threshold serves to determine the countries that fall within or outside the different conditions. It then provides a significant departure from the current SDT time concessions awarded to developing countries by proposing that entry into provisions be made contingent on overcome constraints and not on an arbitrary time period. As way of example, if a country has a calorific supply that is above a given threshold during a period of time, then this may qualify it to leave the group of food insecure countries. This would then mean that the differential treatment applied to this type of countries would cease.

Falling within the purview of this domestic regulatory reform heading lies another justification for SDT that does not necessarily involve institutional constraints or derivatives thereof in applying WTO provisions. The early literature on import substitution identified a set of conditions whereby tariffs could bring about incentives that would stimulate industrial capacity. One could then view applying particular domestic policies such as tariffs or safeguards within the purview of this domestic regulatory reform. Backing to such practices already exists with the use of special safeguard mechanism. It follows that the constraints that need be identified for the application of such SDT would be different but can fall within those identified in Table 1.

#### *External Market Access*

Where access to external markets is concerned (SDT related to market access), it is likely that the above proposed indicators fall short of justifying differential treatment. A move towards competitiveness based indicators like in the EU's GSP schemes can be proposed. Enhanced market access provisions for developing countries would then be contingent on a set of measures that grasp the international competitiveness of a country in a particular good or set of products. Hence countries would lose favourable market access to developed countries once competitive maturity has been gained. One can then measure 'competitive maturity' by way of an array of indicators. The most obvious of these is the RCA, but exclusive use of this indicator would fall short of identifying actual maturity. This indicator would need to be combined with one that identifies both relative and actual market presence. Relative market presence can be measured by using bilateral RCAs, where one compares the market share of imports from a given source to that of the average import source. If the import share of the concerned country is higher than the average import share, the country in question can be said to have a relative bilateral comparative advantage. Where this occurs then it can be said that competitive maturity has been reached. But one also needs to take account the actual market presence. If this competitiveness is reached for one product, but total imports from that source are below a certain threshold, then it can be said that the country in question has not reached an important enough aggregate market presence. SDT on external market issues would then be mediated within a system analogous to that put forward by the EU's GSP where thresholds would determine graduating status across different sectors.

## 4. Method

Identifying the possible constraints that countries face is an important step in the operationalisation of this new concept of SDT, however it is with the more prescient issue of capturing these constraints, by way of analytical criteria, that this section concerns itself. As Stevens (2002) shows, it is unlikely that a single indicator can capture the totality of an identified constraint. Stevens relies on several criteria to capture food insecurity and hence provide lists of countries that could be excluded. But to the extent that several criteria need be used to capture a constraint, then the way that these are combined is likely to matter. This section deals with the methodological hurdles that will be faced in combining identified criteria. We discuss the use of composite indicators and also problems that arise in delimiting thresholds for graduation but before this we identify more general issues that are likely to arise in the application of such an operationalisation.

The use of objective criteria is limited by the availability and quality of data. Despite important efforts made by international organisations, much data for developing countries remains unavailable. Missing country data points will not only lead to indeterminacy in the current condition of a given country, but will also affect results obtained for other countries if ranked criteria are used. The quality of the data and also the consistency of collection methods and homogeneity in the definition of indicators will be important. This issue is best illustrated by way of example. There currently exists an array of measures capturing poverty, each with their own strengths and weaknesses. Poverty indicators can be calculated using either income or consumption based measures and the setting of the appropriate threshold remains a contentious issue in the poverty debate (currently \$1 (ppp) a day is the norm, but many argue that this is imperfect). Measures can also vary in terms of units where poverty can be measured as a headcount or alternatively as an income/consumption gap with respect to the chosen threshold. Whilst the established measure of poverty headcount used by the World Bank would be the obvious choice, it is important to note that there are alternative methods and that the use of one over the other will require judgement and hence will need to be appropriately justified. For the purposes of determining participation in specific WTO provisions it is likely that even the indicators used will have to be determined through a negotiated process.

The indicators used should address the structural aspects of the constraints and hence the temporal volatility of these should be low. One can use averages across time to reduce said temporal volatility which can affect selection into and out of constraints. Trade flows, or some indicators calculated using these suffer such temporal volatility. In recognition to this, the EC graduation threshold needs be surpassed on three consecutive years so that it identifies actual competitiveness and not an outlying one that has arisen through various circumstances. Another indicator, again of competitiveness, that has a great temporal volatility is the RCA indicator when calculated at the product level. The complexity of this indicator makes changes in world exports as well as a particular country's cause great temporal fluctuations and hence this indicator should be used with care. It can be either averaged out across a set period of time or calculated at a fairly aggregate level.

It is also important that any datasets used for these indicators be internationally accepted both in collection methods and in reliability. This will ensure that the process of country selection on the basis of these indicators is accepted by all. It will also minimise possible negative incentives of self-interest in reporting and ensure transparency. To the extent possible one should rely on indicators collected by international organisations.

### **Composite indicators**

The use of a composite indicator can provide a good solution to combining indicators and hence capturing country constraints. (EC, 2005) provides a comprehensive review of the advantages and pitfalls of using composite indicators and Lopez Gonzalez et al (2011) provide an application to the case of pharmaceuticals and TRIPS. Whilst the ability to summarise complex multi-dimensional issues is the main advantage, it does not escape subjectivity or judgement calls. This is true for the initial choice of indicators as for; the choice of weights; the treatment of missing values; and the aggregating technique employed. The problem of missing data is important both in an econometric setting as in one where aggregation is done following a ranking procedure. In an econometric specification, the removal of countries in a sample as a result of missing values can lead to changes in coefficients. This is because the general cause for missing data is non-random and is ingrained in a deeper issue. The lack of data in and of itself may be a symptom of the underlying conditions of the country. Hence missing data is most likely to occur in countries that are vulnerable or that do not have the capacity to collect data. However this generalisation cannot be applied across the board. There will also be countries with available data that are very poor and that have obtained data as a result of technical assistance through the recognition of their lack of capacity. If the lack of data were a symptom of all vulnerable or capacity constrained countries, then this could be used as an indicator in itself but the unobserved heterogeneity suggests a random distribution of missing data need be assumed. If the composite indicator is created using rankings, then any missing data will severely affect its applicability as already discussed above.

The selection of the indicators used to capture the ‘conditions’ that justify the application of SDT which we have discussed at length in this paper will also be subject to criticism. Hence it will need to be appropriately informed and accepted by all signatories. But even once it is accepted, the choice of weights used to combine these and then the thresholds that will determine graduation will also remain contentious. The Commonwealth (1999) study provides a way of estimating weights rather than subjectively choosing them. Although their concern is somewhat different to ours, their methodology is noteworthy. They use economic performance indicators as well as factors relating to natural disasters and geographical characteristics to create a composite indicator of vulnerability. They divide the method into two distinct steps. The first relies on a stochastic econometric model that regresses output volatility, measured in standard deviations, against a set of explanatory variables using weighted least squares (WLS)<sup>22</sup>. These variables capture economic exposure by way of export dependence, export diversification as well as a vulnerability to natural disasters. The regression results

---

<sup>22</sup> The use of WLS is justified by the heterogeneity, in size and behaviour, of the countries in the sample



then give a set of coefficients that determine the weighting structure to the formation of the composite index. The second step is then to apply the data, for a particular country, with the estimated weights to create a vulnerability indicator.

The advantage of this approach is that it identifies the determinants of the outcome variable of interest using statistically sound procedures. However, if the outcome variable of interest is composed of more than one condition, as we saw in the determination of food insecurity in (Stevens, 2002), then further work will need to go into the application of the methodology. Hence, in a hypothetical application of the methodology to (Stevens, 2002)'s example, we would need to define the outcome variable 'food insecurity' using either the daily calorific supply or the share of agriculture in GDP. Trying to combine these indicators into one and then carrying out an econometric analysis would imply making important methodological and theoretical assumption which may not be clear to a non-technical audience. An additional problem in the Commonwealth (1999) study arises from the country selection process. This relies on both the availability of data and on a 'subjective' truncation of the sample. Oil rich Gulf States and transition economies (CIS) are left out of the analysis on the basis of "atypical and, in some cases transient, physical and/or economic characteristics". Leaving countries out of the analysis can be justified for an academic investigation but it cannot be a viable approach to SDT. All countries are atypical and have transient economic characteristics and it is in fact these conditions that we are trying to capture in the operationalisation of SDT. In addition, the use of a WLS method suggests that outliers can have an important influence on the final obtained results hence leaving these countries out in the first place is likely to have affected the coefficients obtained. The likely presence of endogenous independent variables also raises issues with this methodology. The bidirectional causality, which may be present between output volatility and export dependence requires a more formal treatment. It is highly likely that country characteristics are captured in the error term thus biasing the coefficients. Adding to this, such an 'objective' way of choosing weights may be operationally un-implementable in the negotiating process. Allusion is made here to the determination of the different coefficients applied under the Swiss formula for developing country reduction commitments. Past experience in similar issues suggests that any weighting structure proposed is likely to arise through negotiated consent and that an econometric approach, even if found desirable, may prove difficult to negotiate due to the complexity of the method. This again is not dissimilar to the experience seen from the transformation of non-ad-valorem tariffs into ad-valorem equivalents.

The most viable alternative is hence to create a transparent composite indicator where the weighting structure and the thresholds that determine graduation are put under a negotiated process as Lopez Gonzalez et al (2011) suggest. Economists can add to the debate by looking at the sensitivity of an identified constraint to the weights chosen. Much of this is the bread and butter of modelling economists where one assumes a uniform distribution of weights and then one starts giving more (less) importance to some of the indicators that are used to see how the final composite indicator behaves. It is probable that there is a certain degree of correlation between the chosen measures and hence that the weights used affect the final results very little. However the case may be that the correlation is high and hence the weighting structure greatly affects the final outcome. But the advantage of such a system is that it is

transparent and easily replicable. Assuming then that the weights have been given, one need be concerned with setting the graduating thresholds. This is likely to be the most contentious issue in particular for countries that lie near the threshold frontier.

Several thresholds can be invoked. The first is a static and subjective one which is similar to that used by the EU in determining graduation from its GSP preferences. Here the threshold is trade related and set so that countries going beyond a certain market share in the EU three years in succession graduate out of the preferences in a given sector. The 15% market share that the EU uses (12.5% in Textiles) is certainly arbitrary. Given that the GSP system is left to the discretion of donor countries and not binding it can be disputed but ultimately it is the EU's decision. However such static thresholds will need be defensible at the WTO, or also subject to negotiation. Another possibility is that of applying a dynamic or perhaps endogenous threshold. Here countries would negotiate the amount of world trade that can be excluded from general practices and the choice of countries can be made as this is satisfied. Lopez Gonzalez et al (2011) use world trade as well as the amount of trade in pharmaceuticals to determine how these graduating thresholds can affect country selection. Hence if one takes the example of special provisions for food importing countries and the application of subsidies then one can suggest a threshold of countries that compose 20% of world trade as an acceptable exclusion to subsidy measures. One would then use the composite indicator ranking countries to exclude from general provisions the countries who, when ranked, compose a cumulative share of total trade (or agricultural trade) that is of 20% of the world. One of the advantages to this method is that countries would only need to negotiate one number rather than an array. The threshold would be more defensible too as it will be based on negotiated analytical criteria rather than other more arbitrary cut-off points. Another alternative threshold could be one which identifies the number of countries that could be acceptably excluded, from general principles. This would mean that the top x countries, when ranked according to the criteria, would be excluded from the WTO provision under consideration.

## **Final comments**

The evolution of Special and Differential Treatment has transformed an almost fully reciprocal agreement into one where non-reciprocity has become the rule rather than the exception<sup>23</sup>. Irrespective of the justifications or desirability of this, it is undeniable that there are advantages to receiving such treatment which makes its pursuit a common one that can lead to important free-riding. The avoidance of such practices and the need for further considerations for developing country constraints should be reflected in any new forms of SDT.

The nature and scope of SDT has evolved with the progression of ideas, policies and changes in the balance of power. It has moved from a system completely based on exceptions to rules for development objectives; to a more complex toolbox designed to achieve and deal with a wider variety

---

23 An example of such non-reciprocity is the varying tariff reduction commitments across developed and developing countries.

of outcomes. The rise in the number of disciplines under negotiation need be accompanied with a rise in the measure that introduce flexibility.

Whilst we are aware that a generalisation of a concept that is put in place to deal with exceptions does not veer far from an oxymoron it is a crucial step in making the single undertaking more palatable. But exceptions to the rules need be taken at face value. They are not always beneficial to developing countries who can hide behind these to avoid important and much needed trade reforms. Finding the balance between these wrong incentives and spreading the gains from a freer, more integrated world market is the new challenge of the WTO. One that is currently forestalling a negotiated outcome of the Doha round. This then underlines the importance of creating a system for SDT that is acceptable to all parties involved.

We propose one where analytical criteria determine participation in provisions. Such a system is likely to be appropriate for both developed and developing countries. It is likely to take into consideration the important heterogeneity across the self-selecting 'development group' where more advanced economies will graduate into general provisions whilst more targeted flexibilities will be provided to the countries that need them most. Such a system can be fine-tuned to the development concerns of countries whilst also bearing in mind the natural progression in economic development of others.

## **Bibliography**

CARIS. (2010). *Mid-term Evaluation of the EU's Generalised System of Preferences*. Report, Sussex.

Cernat, L., & Mendez Parra, M. (2008, May 21). Aid for trade: How much aid and how much more trade? *International Trade and Finance Association 18th International Conference*. Lisbon, Portugal.

Cottier, T. (2006). From progressive liberalisation to progressive regulation in WTO law. *Journal of International Economic Law*, 1-43.

EC. (2005). *Tools for Composite Indicators Building*. Institute for the Protection and Security of the Citizen, Econometrics and Statistical Support to Antifraud Unit, Ispra.

Garcia, F. J. (2004). *Beyond Special and Differential Treatment*. Boston College Law School.

Hoekman, B., Michalopoulos, C., & Winters, L. A. (2003). Special and differential treatment in the WTO after Cancun. *The World Economy*, 27 (4), 481-506.

Hoekman, B. (2005). Operationalising the concept of policy space in the WTO: Beyond special and differential treatment. *Journal of International Economic Law*, 8, 405-424.

Hoekman, B., & Ozden, C. (2005). *Trade preferences and differential treatment of developing countries: A selective survey*. Washington, DC.: World Bank.

- International Food & Agriculture Trade Policy Council. (2004). *A New Approach to Special and Differential Treatment*. An IPC Position Paper, Washington.
- Kessie, E. (2000). Enforceability of the legal provisions relating to special and differential treatment under the WTO agreements. *The Journal of World Intellectual Property* , 3 (6), 955-975.
- Kleck, A., & Low, P. (2004). *Special and differential treatment in the WTO: Why, when and how?* Geneva: Economic Research and Statistics Division, WTO.
- Lichtenbaum, P. (2001). Special treatment vs. equal participation: Striking a balance in the Doha negotiations. *American University International Law Review* , 17, 1003.
- Lipsey, R. G., & Lancaster, K. (1957). The general theory of second best. *The review of economic studies* , 24 (1).
- Lopez González, J., Méndez Parra, M., Holmes, P. and Shingal, A. (2011). *TRIPS and Special & Differential Treatment – Revisiting the Case for Derogations in Applying Patent Protection for Pharmaceuticals in Developing Countries* (mimeo)
- Matthews, A. (2007). Shallow versus deep special and differential treatment (SDT) and the issue of differentiation in the WTO among groups of developing countries. In J. Morrison, & A. Sarris (Eds.), *WTO rules for agriculture compatible with development* (pp. 79-99). Rome: FAO.
- Michalopoulos, C. (2000). *Trade and development in the GATT and WTO: The role of special and differential treatment for developing countries*. World Bank.
- Page, S. (2004). *The evolution of special and differential treatment in the multilateral trading system*. Workshop, International Centre for Trade and Sustainable Development, Geneva.
- Page, S., & Kleen, P. (2005). *Special and differential treatment of developing countries in the World Trade Organization*. Ministry of Foreign Affairs, Sweden.
- Paugam, J.-M., & Novel, A.-S. (2005). Why and how differentiate developing countries in the WTO? theoretical options and negotiating solutions. *IFPRI/ARD Trade and Development Conference*. Paris.
- Prebisch, R. (1950). The economic development of Latin America and its principal problems. *Bulletin for Latin America* , 7 (1), 1-22.
- Samuelson, P. A. (1962). The gains from international trade once again. *The Economic Journal* , 72 (88), 820-829.
- Scitovsky, T. (1941). A note on welfare propositions in economics. *Review of Economic Studies* , III, 77-88.
- Singer, H. W. (1950). US foreign investment in underdeveloped areas: The distribution of gains between investing and borrowing countries. *American Economic Review* , 40, 473-485.

Stevens, C. (2002). *The future of SDT for developing countries in the WTO*. Sussex: Institute for Development Studies.

Tortora, M. (2003). *Special and differential treatment and development issues in the multilateral trade negotiations: the skeleton in the closet*. Geneva: UNCTAD.

VanGrasstek, C., & Sauve, P. (2006). The consistency of WTO rules: Can the single undertaking be squared with variable geometry? *Journal of International Economic Law* , 9 (4), 837-864.

Wang, Z. K., & Winters, L. A. (2000). *Putting "humpty" together again: including developing countries in a consensus for the WTO*. CEPR Policy Paper.

Whalley, J. (1990). Non-discriminatory discrimination: Special and differential treatment under the GATT for developing countries. *The Economic Journal* , 100 (403), 1318-1328.

Whalley, J. (1999). *Special and Differential Treatment in the Millennium Round*. Coventry: Universities of Warwick and Western Ontario and NBER.