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IMPACT ASSESSMENT

VOL. I

Accompanying the document

Proposal for a

REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

on applying a scheme of generalised tariff preferences

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(*This report commits only the Commission's services involved in its preparation and does not prejudge the final form of any decision to be taken by the Commission'*).

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1. PROCEDURAL ISSUES AND CONSULTATION OF INTERESTED PARTIES

1.1. Background

The Generalised System of Preferences (hereinafter 'the scheme') helps developing countries, particularly Least Developed Countries (hereinafter 'LDCs'), reduce poverty by generating or increasing their revenues from international trade. It does so by providing import preferences. On top of this central goal, the scheme has taken up an additional role. This is to provide incentives, in the form of additional import preferences, to those countries committed to promote sustainable development and good governance.

The scheme represents a departure from the most-favoured nation principle under the General Agreement on Tariffs and Trade (GATT) in favour of developing countries. It therefore has to comply with the terms and conditions of the 'Enabling Clause' (officially called the 'Decision on Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries'), which allows World Trade Organization's (WTO) Members to accord different and more favourable treatment to developing countries provided the treatment is 'generalized, non-reciprocal and non-discriminatory'.

In addition to the EU, eight developed countries (Australia, Canada, Japan, New Zealand, Norway, Switzerland, Turkey, and the US) have accepted the United Nations Conference's on Trade and Development (UNCTAD) recommendation of 1968 to grant autonomous trade preferences to developing countries by offering their own schemes for a generalised system of preferences[1].

First introduced in 1971, the scheme currently aims to achieve the objectives set out in the *Communication from the Commission to the Council, the European Parliament and the Economic and Social Committee on the function of the Community's Generalised System of Preferences for the ten year period from 2006-2015*[2] (these objectives are fully described in §3.2).

The scheme[3] grants preferential access to EU markets on a generalised and non-discriminatory basis to 176 eligible countries and territories and is made up of three arrangements:

- the general arrangement (hereinafter 'GSP');
- the special incentive arrangement for sustainable development and good governance (hereinafter 'GSP+'), which offers additional preferences as incentives to support vulnerable developing countries in ratifying and effectively implementing 27 international conventions on human and labour rights, the environment and good governance;
- the Everything But Arms arrangement (EBA), which provides duty-free, quota-free access to LDCs.

[1] As of 1 January 2011 the US GSP scheme has lapsed, pending extension approval by US Congress.
[2] COM (2004) 461 final, hereinafter 'the Commission GSP Communication.'
[3] For a detailed description of the scheme, see Annex 1.

The present scheme has been implemented through successive regulations each applying for three year periods, to ensure that it can be updated on a regular basis so as to take account of evolutions in relevant trade data. The current scheme was established by Council Regulation (EC) No 732/2008[4] that entered into force on 1 January 2009 and expires on 31 December 2011. On 26 May 2010 the Commission adopted a proposal to extend the validity of this regulation to 31 December 2013, in order to allow time to prepare the revision of the scheme. (The proposal has been sent to the Council and the European Parliament (EP) for adoption[5].) However, the new, longer decision-making procedures envisaged in the Lisbon Treaty make it advisable to move from a scheme implemented in three-year cycles to a scheme with an open-ended duration. This ensures that reviews of the scheme do not impinge upon the predictability economic operators hold essential.

A recently completed mid-term review provides the background for the planned Commission proposal for a revised regulation to replace the existing scheme upon its expiry in December 2013. Both the EBA arrangement and the rules of origin provisions, fall outside the scope of this revision: the former, because it is not subject to periodic reviews; and the latter, because new legislation on rules of origin has entered into force in 2011.

1.2. Organisation and timing

The Directorate-General for Trade is the lead service in the case of a proposal for a regulation applying a scheme for a Generalised System of Preference. This proposal is part of the Commission's work programme for 2010/2011 (31.3.2010 COM (2010) 135 final).

The other DGs and services that have been involved in the preparation of the impact assessment are: DG Agriculture and Rural Development, DG Budget, DG Economic and Financial Affairs, DG Employment, Social Affairs and Equal Opportunities, DG Enterprise and Industry, DG Environment, DG Maritime Affairs and Fisheries, DG Development, DG External Relations (now EEAS), European Anti-Fraud Office, Eurostat and the Secretariat-General.

An inter-service steering group was set up for this impact assessment and met on 10 March, 4 June, 8 and 24 September and 18 October 2010. An additional meeting took place on 25 February 2011.

1.3. Consultation and expertise

This impact assessment report has been prepared following consultations[6] with Member States and other stakeholders (including civil society, industry, beneficiary countries, the EP and WTO members). These consultations were launched following the *Stakeholder Conference on EU Trade Policy towards Developing Countries* on 16 March 2010. A web-based consultation (i.e., an online questionnaire) was open to the public from 27 March to 4 June 2010. In total, 143 exploitable answers were received

[4] OJ L 211, 6.8.2008, p.1.

[5] Following entry into force of the Lisbon Treaty, measures defining the framework of the common commercial policy are adopted by the European Parliament and the Council acting jointly under the ordinary legislative procedures; previous GSP regulations were decided by the Council alone.

[6] The GSP Consultation Report and the full list of answers are available at: http://trade.ec.europa.eu/consultations/?consul_id=142

from representatives of both beneficiary and non-beneficiary countries, business associations, trade unions, research centres, non-governmental organizations, private companies and individuals. In parallel to the on-line consultation, specific outreach activities were organised, such as: an information meeting for WTO Members in Geneva on 5 May 2010; consultations with GSP beneficiary countries on 18 May 2010; a civil society meeting in Brussels on 26 May 2010; and a meeting with EP representatives on 2 June 2010. EU Delegations were asked to disseminate information on the GSP review process in their respective countries.

In general the consultations underlined the importance of the scheme for its users. Almost all respondents agreed that the scheme was still a valid trade instrument for developing countries. Respondents from different beneficiary countries confirmed that the scheme had played an important role in the expansion and diversification of their trade sector. About half of the respondents, representing different types of stakeholders, stressed the need for modifications covering: stronger control and verification of requirements to ensure that preferences go to the countries in need; support for investment in developing countries; competitiveness of EU industries; and focus on abolishing restrictions in international trade and lowering of custom duties and other barriers.

The views of stakeholders were taken into account in preparing this impact assessment, as is highlighted in several instances in the analysis that follows. The Commission's minimum standards for consultations were met. A summary of the consultation report is presented in Annex 2.

To assess the extent to which the EU's scheme meets the need of developing countries, a mid-term evaluation was carried out by an external contractor, the Centre for Analysis of Regional Integration at Sussex (CARIS). The final report was published on 26 May 2010 on the DG Trade website[7]. The results of this study are reflected in this impact assessment where relevant, and in addition an executive summary is presented in Annex 3.

1.4. The opinion of the Impact Assessment Board

On 19 November 2010 the Impact Assessment Board of the European Commission delivered its opinion regarding preliminary version of this Impact Assessment report. Following the recommendations of the Board, the report has been redrafted along four main lines.

1. The analysis of problems has been (i) strengthened on the basis of a significant *corpus* of evidence, and (ii) structured around a problem chart and problem tree which clearly identify problems and their drivers, as well as the operational, specific and general objectives to be achieved.

2. The range of options and sub-options has been extended from 3 to 6, and these have been compared against a baseline. The baseline has considered a short-run scenario (current level of preferences) and a long-run scenario (level of preferences reflecting the successful conclusion of the on-going bilateral and multilateral negotiations). This

[7] http://trade.ec.europa.eu/doclib/docs/2010/may/tradoc_146196.pdf

means that 12 different possibilities have been analysed in order to shed light on all the salient issues linked to the scheme.

3. The analysis of impacts systematically includes the full range of variables suggested by the Board, and the comparison of the options has been based on the required efficiency, effectiveness and coherence criteria.

4. The structure of the report has been streamlined, and the largely expanded annex section has been organised in a systematic, user-friendly manner.

2. PROBLEM DEFINITION[8]

2.1. Introduction

Though some have questioned whether tariff preferences have actually made a substantive difference in terms of enhancing the welfare of beneficiary countries, the analysis of the effectiveness of the existing GSP scheme undertaken by CARIS, concluded that the scheme has been generally successful. That view is echoed by the vast majority of responses to the consultation, which confirmed that the scheme and its objectives remain valid. It is further underlined by the figures in the CARIS study showing the importance of the preferences. Imports benefiting from preferences are significant (see Annex 4, Table 4-1). They amounted to almost €60 billion in 2009. This corresponds to over 9% of total EU imports from all beneficiaries. This percentage varies across categories of beneficiaries. Preferential imports account for 8% of total imports from GSP countries, for 20% of total imports from GSP+ countries, and for 32% of total imports from EBA beneficiaries. Considering that a vast majority of imports from beneficiaries (62%[9]) are subject to 0% general tariffs,[10] a more accurate picture is given by expressing preferential imports as a percentage of total imports for which the default tariff rate would be positive. Thus expressed, GSP imports represent 21% of goods that are capable of enjoying preferences, GSP+ imports account for 63%, and EBA imports account for 67% (see Annex 4, Table 4-3).

The CARIS study[11] also highlights the fact that growth in trade and investment with the EU in recent years has been significantly higher for GSP beneficiary countries than for non-beneficiaries. Preferential exports under the scheme have increased, and have done so at a faster rate than that of other exports to the EU. Therefore, the scheme has become an engine for total export growth for beneficiaries. This engine effect is particularly remarkable for EBA countries, for which the whole of the increase in exports to the EU is due to exports of goods under preferences. The scheme's preferences appear to be critical particularly for GSP+ and EBA countries.

The general attractiveness of the scheme is also underlined by a relatively high level of utilisation of the available preferences[12], but with room for further improvement:

[8] Further details and evidence regarding the problem definition are provided in annex 7.
[9] See Annex 4, Table 4-2.
[10] These are the so-called "most favoured nation" tariffs (hereinafter "MFN"), which apply to all WTO members as a rule.
[11] CARIS, page 9.
[12] This is confirmed by CARIS, see Ibid.

53% for GSP countries, 69% for EBA countries and 85% for GSP+ countries (see Annex 4, Table 4-7).

The system provides real gains for exporters, who appear to benefit from roughly half of the excess gains (the other half accruing to importers in the EU)[13]. These gains are significant. An indication of their order of magnitude is the amount of unpaid import duties *per annum*, which – other things being equal – would be of the order of €2.1 billion (based on 2009 figures, the latest available data).

In respect of the second goal of the EU's scheme, i.e., the promotion of sustainable development and good governance, there is evidence that the GSP+ arrangement has had a positive impact on the ratification of GSP+ related conventions, thus encouraging the further inclusion of developing countries into the international community. However progress in actual effective implementation of the relevant conventions is less evident, although some GSP+ beneficiary countries have undertaken substantial reform efforts. The monitoring bodies of the relevant conventions have noted a number of positive developments, including the adoption of legislative and policy measures taken with a view to implement conventions.

2.2. Overall framework and constraints external to the scheme

Development and poverty reduction are complex goals, which necessitate many building blocks to be achieved. The scheme is one of those many blocks. While, on its own, the scheme will not directly reduce poverty, its preferences can help developing countries boost exports and develop new industries – a factor which, given an adequate political and economic context, can contribute significantly towards development and poverty reduction.

The potential benefits of the scheme are subject to various structural and other constraints. The scheme operates in a complex context, where it interacts with a number of policy strands and economic realities. The latter place constraints on the scheme, and in turn the scheme affects other strands of EU policy.

The first constraint arises due to the EU's low level of tariffs (for example, in 11 out of 21 product categories, general tariffs are 3,5% or lower[14]) and the significant number of tariff-free lines (25% of the total EU tariff lines[15]), which limit the scope and size of preference margins and, thus, set a limit on the possible impact of the GSP scheme. As multilateral and bilateral negotiations progress, tariffs (and thus preference margins) will continue to decrease.

The CARIS study underlined that a second cause of the preference utilisation gap is bureaucracy in the exporting countries[16]. This aspect can be addressed by trade facilitation initiatives, for example in the context of *Aid for Trade*.

A third constraint is the existence of parallel preference schemes such as the EPA Market Access Regulation[17] (a program under which the EU grants preferences to

[13] Ibid.
[14] See Annex 4 Table 4-10.
[15] See Annex 4, Table 4-5.
[16] See CARIS, page 81.
[17] Council Regulation (EC) No 1528/2007 of 20 December 2007, (OJ L 348, 31.12.2007, p. 1).

Cotonou Agreement parties that have initialled by 31 December 2007 an Economic Partnership Agreement with the EU prior to its signature and provisional application). The impact of such schemes can be roughly measured by the level of EBA imports entering under such parallel schemes – almost 7%[18] of the total. However these are temporary and should disappear once EPAs enter permanently into force.

In relation to the GSP+ arrangement, there are several further problem drivers that fall outside the remit of the scheme. The scheme's preferences are not supposed to 'compensate' for the eventual cost of implementing conventions, but rather to provide an incentive for countries to sign up to relevant international conventions and submit to the monitoring and reviews under them. But this does not mean that implementation costs are low – in fact these may be significant in some cases[19]. In a context where the necessary data for a meaningful cost-benefit analysis is lacking[20], such costs should not be underestimated.

In addition, the success in implementing the relevant conventions depends greatly on domestic political dynamics within the countries concerned. Government priorities, budgetary constraints, availability of appropriate development and technical assistance will be powerful determinants of actual progress, irrespective of the preferences involved. Significant changes in the fields related to GSP+ conventions typically take time to materialise[21]. Therefore, ambition in this area must be tempered with realism: the scheme will help given time, but it cannot lead alone to the achievement of sustainable development and good governance, which ultimately depends on outside structural factors.

Finally, the GSP+ eligibility requirement related to promotion of sustainable development and good governance is based on the ratification and implementation of 27 international conventions, which are defined and monitored by international bodies (UN, ILO…). Therefore in its assessment concerning implementation of conventions the EU relies on available recommendations by the relevant monitoring bodies. This implies limitations as to timing (in most cases the monitoring work is not done every year) and substance (what some may see as a breach of core conventions may not be the international institutions' view).

2.3. Problems that impinge upon the scheme's effectiveness/efficiency

The scheme is technically complex and involves a large set of diverging interests both in the EU (supplying countries, competing producers, importers…) and among the scheme beneficiaries (who compete against each other). The salient issues and problems that can not be solved by the scheme are described in Annex 5.

Issues which represent genuine problems that can be addressed in the review process have been identified and will be described below. They are depicted in the following problem chart and problem tree.

[18] See Annex 4, Table 4-2.
[19] See CARIS, pages 10-11. The consultation process also highlighted this point.
[20] See CARIS, page 172.
[21] CARIS found that it was too early to judge on whether GSP+ had been effective in terms of implementation of conventions; see page 10.

Problem chart

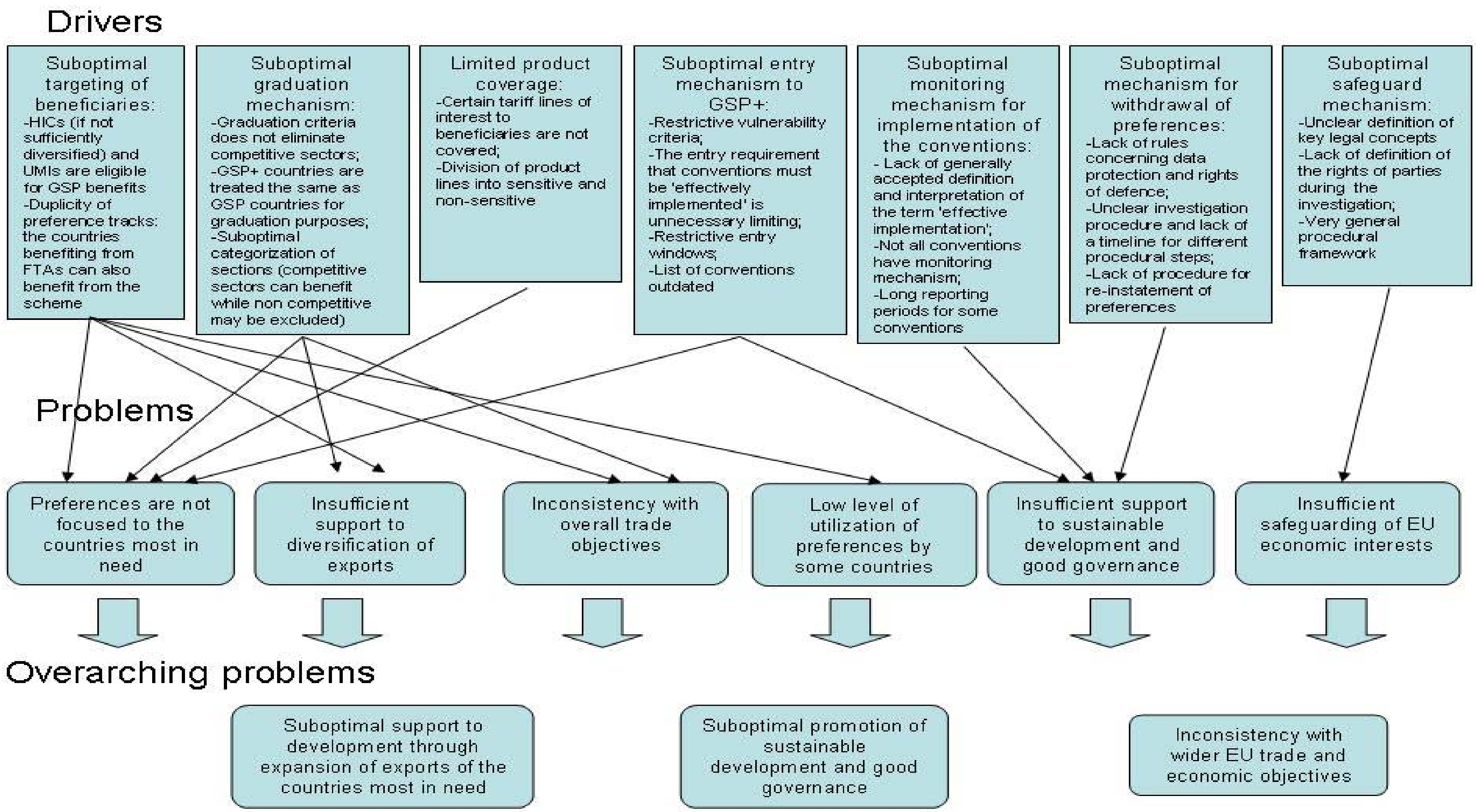
(Note: grey areas denote problems external to the scheme)

Problems	Problem drivers	Operational objectives	Specific objectives						General objectives		
			S-1	S-2	S-3	S-4	S-5	S-6	G-1	G-2	G-3
			Better focus the preferences on countries most in need	**Remove disincentives to diversification**	**Enhance consistency with overall trade objectives, whether bilateral or multilateral negotiations**	**Strengthen the support for sustainable development and good governance**	**Improve the efficiency of safeguard mechanisms**	**Enhance legal certainty, stability and predictability**	**Contribute to poverty eradication by expanding exports of countries most in need**	**Promote sustainable development and good governance**	**Ensure better safeguard for EU's financial and economic interests**
The preferences are not focused to the countries most in need	**Suboptimal targeting of beneficiaries** -High income countries (if not sufficiently diversified) and upper middle income countries are eligible for GSP benefits	Revise the beneficiary country list by deferring benefits to those countries that do not need preferences	X	X	X				X	X	X
	-Duplicity of preference tracks: FTA partners are GSP beneficiaries even though they already benefit from preferences under FTA	Revise the beneficiary country list by deferring benefits to those countries that do not need preferences	X		X			X	X	X	X
	Suboptimal graduation mechanism -Large competitive pressure by GSP beneficiaries on GSP+ and EBA countries -Graduation criteria do not eliminate competitive sectors -GSP+ countries are treated the same as GSP countries for graduation purposes	Target graduation on the prime beneficiaries ensuring that GSP preferential rates are withdrawn from competitive products	X		X				X	X	X
	-Suboptimal categorization of sections (competitive sectors can benefit while non competitive may be excluded)	Redefine product sections to reflect more homogeneous product categories	X		X			X	X	X	

	Limited product coverage -Certain tariff lines of interest to beneficiaries are not covered -Division of product lines into sensitive and non-sensitive	Revise the product coverage and analyze the impacts	X			X			X	X	
	-Restrictive GSP+ vulnerability criteria	Broaden vulnerability criteria	X	X		X			X	X	
Low level of utilization of preferences by some countries	-Low level of existing MFN duties, few tariff peaks lead to low preferences -Existence of other preferential arrangements (EPA Regulation,) Bureaucracy in the exporting countries -Large competitive pressure by GSP countries on GSP+ beneficiaries and LDCs -Duplicity of preference tracks: FTA partners are GSP beneficiaries even though they already benefit from preferences under FTA	Revise the beneficiary country list by deferring benefits to those countries that do not need preferences	X	X	X				X	X	X
Ineffective support to diversification of exports	-Low level of existing MFN duties, few tariff peaks lead to low preferences -Large competitive pressure by GSP beneficiaries on GSP+ and EBA countries -High income countries (if not sufficiently diversified) and upper middle income countries are eligible for GSP benefits	Revise the beneficiary country list by deferring benefits to those countries that do not need preferences	X	X	X				X	X	X
	-Graduation criteria do not eliminate competitive sectors -GSP+ countries are treated the same as GSP countries for graduation purposes	Target graduation on the prime beneficiaries ensuring that GSP preferential rates are withdrawn from competitive products	X		X				X	X	X
Insufficient support to sustainable development and good governance	**-Sub-optimal entry mechanism to GSP+:** -Significant implementation costs for beneficiaries -Domestic beneficiary politics not always conducive to scheme's goals -Restrictive vulnerability criteria	Broaden vulnerability criteria	X			X		X	X	X	

	-The entry requirement that conventions must be 'effectively implemented' is unnecessary limiting -Restrictive entry windows -List of conventions outdated	Simplify GSP+ entry mechanism	X		X	X		X	X	X	X
	Suboptimal monitoring mechanism for implementation of the conventions -Not all conventions have monitoring mechanism -Long reporting periods for some conventions -Lack of generally accepted definition and interpretation of the term 'effective implementation'	Develop a more effective and transparent mechanism for monitoring and evaluating the GSP+ countries' commitment and progress in the implementation of GSP+ conventions			X	X		X		X	X
	Suboptimal mechanism for withdrawal of preferences -Lack of rules concerning data protection and rights of defence -Unclear investigation procedure and lack of a timeline for different procedural steps -Lack of procedure for re-instatement of preferences	Develop credible and efficient procedures for temporary withdrawal of the preferences and procedures for renewal of the preferences	X		X	X		X	X	X	X
Insufficient safeguarding of EU economic interests	**Suboptimal safeguard mechanism** -Unclear definition of key legal concepts -Lack of definition of the rights of parties during the investigation -Very general procedural framework	Improve the administrative procedures of safeguard mechanisms					X	X			X
Inconsistency with overall trade objectives	**Suboptimal targeting of beneficiaries** -High income countries (if not sufficiently diversified) and upper middle income countries are eligible for GSP benefits -Duplicity of preference tracks: FTA partners are GSP beneficiaries even though they already benefit from preferences under FTA	Revise the beneficiary country list by deferring benefits to those countries that do not need preferences	X	X	X				X	X	X
	Suboptimal graduation mechanism -Graduation criteria do not eliminate competitive sectors -GSP+ countries are treated the same as GSP countries for graduation purposes	Target graduation on the prime beneficiaries ensuring that GSP preferential rates are withdrawn from competitive products	X		X				X	X	X

Problem tree



2.3.1. *The preferences are not focused to the countries most in need*

Suboptimal targeting of beneficiaries

The first question when examining the scheme is whether the beneficiaries are well targeted. In the public consultation, the majority of opinions recommended that the EU should concentrate the scheme primarily on countries 'most in need'. This concept is not explicitly laid out in any legal text, but can be described by combining a 'positive' approach (which countries have trade, financial and development needs that should be addressed by the scheme) and a 'negative' approach (which countries don't have such a level of needs).

Positive approach: The current scheme identifies two specific categories of countries with such needs. The first category comprises LDCs as defined by the UN. They are poor and receive special EBA treatment. The second category contains vulnerable countries (they lack diversification and are insufficiently integrated into the international trading system). Vulnerability is a pre-condition for receiving special GSP+ treatment, whilst eligibility depends on prior ratification and effective implementation of the relevant conventions. The consultation responses have underlined that there is substantial support for maintaining the current treatment for these countries, underlining that they are 'most in need'.

Negative approach: There are a number of countries that do not have trade, financial and development needs that the scheme is intended to address. This is one of the key problems with the scheme, as described below.

The CARIS analysis suggests that under the current scheme a large degree of competitive pressure for LDCs (and GSP+ beneficiaries) comes from GSP beneficiaries. GSP beneficiaries account for 81% of preferential imports, GSP+ countries for 9%, and LDCs countries for 10% (see Annex 4, Table 4-1). This is not surprising, as the five largest exporters covered by the GSP scheme (China, India, Thailand, Brazil, Russia) account for more than 67% of all GSP covered imports. It should be underlined that this is not only the result of the economic size of beneficiaries. The share of imports under the scheme for five (China, Brazil, India, Thailand and Indonesia) out of the top six GSP beneficiaries (the foregoing plus Russia) is significantly higher than their share in *total* imports (see Annex 1, Table 1-2).

There are several factors that promote this asymmetry. First, several countries classified as high-income countries (HICs) by the World Bank[22] continue to be beneficiaries[23], as they are not 'sufficiently diversified'. However, as such countries have the resources to attain higher levels of diversification without the help of EU preferences, retaining them in the scheme must be questioned.

[22] Countries are divided according to 2009 GNI per capita, calculated using the World Bank Atlas method. The groups are: low income, $995 or less; lower middle income, $996 - $3,945; upper middle income, $3,946 - $12,195; and high income, $12,196 or more. For the purpose of this assessment, countries must be classified in the last 3 years available as HIC

[23] Aruba, Bahamas, Bahrain, Barbados, Bermuda, Brunei Darussalam, Cayman (Islands), French Polynesia, Greenland, Guam, Kuwait, Macao, New Caledonia, Northern Mariana Islands, Oman, Qatar, Saudi Arabia, the Netherlands Antilles, Trinidad and Tobago, United Arab Emirates, Virgin British (Islands). All of these countries have been classified as HIC in the last 3 years available.

The same phenomenon arises with other countries whose levels of wealth and development are high[24]. This is the case for 31 so-called Upper Middle Income countries[25] (UMIs) according to the same classification by the World Bank. These countries also have significant per capita income levels – so much so that they are in the same category as EU Member States such as Bulgaria and Romania. They also include economies which have successfully completed their transition from centralised to market economies.

The use of preferences by HICs and UMIs increases the competitive pressure on exports from poorer, more vulnerable countries, whose needs are far greater and thus deserve increased attention.

Those countries that already profit from preferences via another bilateral preferential arrangement with the EU also continue to benefit from the scheme. Currently this set comprises 23 beneficiary countries and additional 8 partners will do so when they have concluded agreements with the EU (see Annex 1 Table 1-1). These countries choose to use preferences either under the bilateral preferential arrangement or under the scheme. This choice of preference channels generates additional customs procedures affecting the transparency of offered preferences and it is thus not efficient. This is why a majority of respondents in the consultation process supported the principle to remove such countries from the scheme[26].

The current regulation already establishes that preferential trade agreement partners should be removed from the scheme provided the agreement covers all the preferences offered by the scheme. But this principle is not enforced because of uncertainty about whether (it is possible to determine that) *all preferences* have in fact been covered when the rules of origin differ in either case. The duplication of preferences for a single exporter creates inefficiencies which will only balloon as new agreements are concluded with the 78 partners with whom the EU is currently negotiating bilateral deals (see Annex 1 Table 1-1).

In short, HICs, UMIs, and countries benefiting from another bilateral preference arrangement covering substantially all preferences provided under the scheme should not be considered as being countries most in need or sharing the same development, trade and financial needs as the remaining developing and vulnerable countries.

Suboptimal graduation mechanism

Not all developing countries are the same. In particular, a significant number of developing economies have generated certain export-oriented manufacturing sectors which have successfully penetrated world markets. Advantages based on low labour costs and economies of scale, and specialising in products that exploit such advantages, have made a number of

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[24] A number of different (and largely convergent) indices exist to identify them. For the purpose of this impact assessment we will use the same World Bank classification, which is based on *per capita* income—the index preferred by a majority of respondents to the consultation.

[25] American Samoa, Antigua and Barbuda, Argentina, Belarus, Botswana, Brazil, Costa Rica, Cuba, Dominica, Fiji Islands, Gabon, Grenada, Jamaica, Kazakhstan, Lebanon, Libyan (Jamahiriya Arab), Malaysia, Mauritius, Mexico, Mayotte, Palau, Panama, Russia, Saint Lucia, Saint-Vincent-et the Grenadines, Seychelles, South Africa, St. Kitts and Nevis, Suriname, Uruguay and Venezuela. All of these countries have been classified as UMI in the last 3 years available.

[26] A number of respondents in the consultation process wished to see both preferential channels (PTA and the scheme) maintained. The reason for this was the strictness of the scheme's preferential rules of origin, as compared to those under a PTA. Now that the rules of origin applicable to the scheme have been relaxed this reason loses much (if not all) of its relevance.

sectors highly competitive at world level. These sectors are typically located in 'emerging' economies such as China, India, and the more advanced Southeast Asian economies.

These sectors receive benefits under the scheme, although arguably they no longer require preferences to achieve a substantial presence in the EU (or indeed in world markets). Indeed, such competitive sectors are placing EU industry under pressure, and this is partly due to the preferences they enjoy. Moreover, the speed of progress by 'emerging' countries and the presence they have achieved in certain sectors via economies of scale (e.g., sheer *size*) generate *de facto* 'barriers' to entry for the less advanced—which need increasing efforts to diversify their export base[27].

For example, India's share in the pool of total imports which are *eligible* for preferences is 7%. One would expect that India's share in the imports which *actually receive preferences* would be of the same order of magnitude. But the figure is actually 22%, so India takes more preferences than the size of its exports would indicate. But India is no exception: out of the top six GSP beneficiaries, all of which belong to this 'emerging' category, four others (aside from India) are exactly in this situation. This means that some other country is receiving *proportionally less preferences* than their expected share (see Annex 7, indent 6).

The scheme has a mechanism to weed out competitive sectors from specific countries and withdraw preferences—the graduation mechanism[28]. Under the current scheme the graduation mechanism has been barely used. Out of a total of over 2400 country-sectors[29], only 20 have been graduated—13 of which are Chinese sectors (see Annex 1 Table 1-4). This indicates that the current graduation mechanism is insufficiently responsive to ensure the effectiveness and efficiency of the scheme for those countries-sectors which genuinely need preferences to expand their export base and volume. Here, the term 'country-sector' is emphasised, as there are many sectors in different emerging economies which are insufficiently competitive and should thus continue to enjoy preferences.

Another important inadequacy of the graduation mechanism is that graduation is based on the categories of the sections of the EU Customs Tariff. While administratively easier to manage and more stable for economic operators, the categories are so large that they include in some cases heterogeneous products.[30] For example, the umbrella and footwear industry are treated as one, so are rubbers and plastics, fish and meat, edible and non-edible vegetables, tobacco and other prepared foodstuffs. This leads to a situation where products that are not necessarily competitive are excluded just because they fall in a category where products from a totally different, highly competitive industry predominate.

Finally, as has been noted by many stakeholders in the consultation process, the current scheme does not ensure equal treatment for EBA and GSP+ countries. Graduation applies to GSP+ countries but not to EBA countries; and this, even where GSP+ countries share a very similar economic profile (i.e., vulnerability because of a low, non-diversified export base)[31].

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[27] See for example, Paul Collier, The Bottom Billion, page 10 and pages 166-168.

[28] Graduation means that imports of particular groups of products (listed as one section in the EU Customs Tariff) from a given GSP beneficiary country lose GSP or GSP+ preferences when the average imports of a section from a country exceed 15% of GSP imports of the same products from all GSP beneficiary countries during three years (the trigger is 12.5% for textiles and clothing). Se Annex 1.

[29] 127 non-EBA beneficiaries (EBA can not be graduated in the EU’s scheme) times 19 sectors with preferences.

[30] For further details see Annex 1 Table 1-5.

[31] See Annex 1 Table 1-1 (virtually all EBA countries are vulnerable).

Insufficient product coverage
One of the most controversial aspects of the scheme is its product coverage, as shown by the particularly contradictory views emanating from the consultation process[32]. Many have argued that the countries most in need fail to gain access to the EU market because the products they would be most likely, or would most want, to export are not covered by the scheme.
First, although the scheme has broad product coverage, still it is not complete**.** Approximately 66% of the EU's 9443 tariff lines enjoy preferences for GSP and GSP+ countries, and the figure is 75% for EBA. In other words, as 25% of tariff lines are duty free to start with, for GSP and GSP+ beneficiaries, 91% of tariffs lines are either preferential or duty free, and basically 100% for EBA (Annex 4, Table 4-4). Thus, there is still scope for extension: product coverage may be opened up to a further 40% of agricultural lines, 1% of textile products and 2% of industrial products.

Second, another *de facto* limitation of the product coverage is division of product lines into sensitive and non-sensitive ones: non-sensitive products enjoy duty-free access and sensitive products (a mixture of agricultural, textile, clothing, apparel, carpets and footwear items) benefit from a tariff reduction of 3.5 percentage points on *ad valorem* duties compared to the standard MFN tariff. For GSP beneficiaries 61% of the tariff lines covered are sensitive, accounting for 63% of covered imports.

2.3.2. Insufficient support to diversification of exports

Initially, the original goal of generalised preference schemes was to help developing economies increase their industrial exports. The premise was that their economies were too dependent on commodities (particularly agricultural ones), and would benefit from industrialisation. Providing preferences in industrial products would help boost such exports and contribute to diversification through the development of a broader industrial base.

However the scheme's contribution to diversification has been mixed. The CARIS study noted that, when all beneficiaries and products are taken together, the evidence for diversification is limited to products with low preference margins[33]. Why? As explained above, the bulk of exports under the scheme come from emerging economies. These have based their success on diversification into industrial products which are subject to low import duties into the EU—and thus low preferences. Contrary to the picture for emerging economies, the scheme has not provided sufficient support for diversification amongst poorer beneficiaries (LDCs).

For example, compared to GSP beneficiaries, EBA countries enjoy significant (additional) preferences in only 7 out of 21 sectors (mainly agricultural, textile and footwear products), and in only 4 when compared to GSP+ countries (only agricultural products). In other words, for a significant amount of products, and in particular for industrial products, the scheme may not provide significant preferences to LDCs with respect to more developed GSP+ or GSP competitors.

The inclusion in the current scheme of GSP countries that scarcely qualify as countries most in need (HICs and UMIs) and which exert significant pressure on competing EBA and GSP+

[32] Also by the attention paid to this by a number of Member States which support a very broad extension of the product coverage.
[33] See CARIS, pages 63-66.

products in the scheme – as well as the relatively weak graduation mechanism – makes diversification in poorer and vulnerable countries more difficult to achieve because the GSP countries capture much of the preferences, particularly in industrial products. It thus impinges significantly upon the effectiveness of the scheme as regards diversification.

2.3.3. Inconsistency with overall trade objectives

The scheme is an autonomous measure with its own developmental and trade objectives. While these are fully independent from EU negotiation goals in the bilateral or multilateral arena, the scheme has side effects on such goals. Therefore, these must be described for the purpose of the impact assessment.

The Commission’s recent communication on the future of trade policy underlines the importance of the conclusion of bilateral and multilateral negotiations. The EU is engaging in bilateral negotiations with many of the scheme's beneficiaries (currently 78 countries). It could be argued that the existence of preferences render negotiations more difficult, but the recent conclusion of ambitious free trade agreements with partner countries which benefit from EU preferences under the GSP+ scheme show that this potential problem is not insurmountable.

It is equally clear that in view of the GSP scheme's goal, which is to provide preferences that respond positively to the trade, financial and development needs of beneficiaries, the impact which these potential difficulties can have on trade negotiations is simply irrelevant.

However, as explained above, the current scheme is not well targeted and provides preferences to countries which do not need them to the same extent. Thus, while the objective of focusing the benefits of the GSP scheme on those countries which need it most has nothing to do with other trade negotiations, it might still have the unintended consequence of providing more advanced developing countries with a greater incentive to enter into and conclude reciprocal trade negotiations with the EU.

This may not have a detrimental impact on those countries even from the point of view of development policy, since such preferential agreements provide much broader advantages to our trading partners. They cover not only tariffs for certain goods, but many other aspects where trade is liberalised. Moreover, they provide a permanent contractual framework which the EU can not revoke unilaterally, thus enhancing legal security and promoting stability and predictability for exporters.

2.3.4. Low level of utilization of preferences by some countries

The first problem driver which can be changed within the scheme is the existence of a choice of preference tracks for preferential trade agreement partners. This driver has been explained above, and it reduces preference utilisation almost automatically.

The second driver is the competitive pressure exerted by GSP countries on GSP+ beneficiaries and LDCs. Typically, large-scale exporters located in GSP countries are prime suppliers to EU importers and distributors. For non-sensitive products, this 'competitive advantage' of GSP exporters is gained partly at the expense of LDCs or GSP+ countries, which derive (relatively) less benefit from GSP preferences to which in principle they have an equal entitlement. Inevitably, this turns LDC suppliers into residual suppliers, which export relatively small shipments to the EU, irregularly. Given the relatively small size value of such transactions, importers have less incentive to bear the costs necessary to claim preferences (e.g., obtaining and administration of origin certificates). So, in the end, many preferences are simply not utilised.

2.3.5. *Insufficient support to sustainable development and good governance*

According to the Commission's draft report on the status of ratification and available recommendations by the relevant monitoring bodies[34], beneficiary countries generally comply with requirements regarding the effective implementation of GSP+ conventions. However, it should be noted that the monitoring bodies have drawn attention to certain, in some cases serious, shortcomings concerning legislative alignment with the conventions and implementation of the conventions in practice, as well as to delays in reporting to the monitoring bodies by most beneficiary countries[35].

The public consultation made clear that GSP stakeholders have high expectations to make the scheme a more effective tool for sustainable development and good governance; particularly through better defined conditions of access to the GSP+ scheme and a more transparent and comprehensive assessment of the level of compliance with the GSP+ eligibility criteria.

There are several problem drivers that can be addressed to make GSP+ arrangement more effective in supporting sustainable development and good governance.

Suboptimal entry mechanism to GSP+

First, excessively restrictive vulnerability criteria prevent several poor countries from applying for the GSP+ arrangement. The CARIS analysis[36] indicates that the current vulnerability criteria (low share in GSP imports and small diversification of exports) that determine eligibility for GSP+ leave some vulnerable countries no possibility to qualify. Also, during the consultation process many stakeholders expressed the desirability of redefining the criteria to allow for further potential applicants.

Such restrictive approach limits the extent to which GSP+ promotes sustainable development and good governance, in the sense that amending the vulnerability thresholds so as to enlarge the field of potential applicants can be an incentive for a greater number of countries to ratify and implement international rules and standards and engage in internal reforms.

Second, the condition for access to GSP+ – that the country has not only ratified, but also 'effectively implemented' the conventions – is unnecessarily limiting; it does not as such support the incentive based nature of the scheme[37]. Therefore, the challenge for the revised regulation is to define an approach that better reconciles with the incentive to adhere to international instruments.

Third, the existence of entry windows (open only once every 18 months) prevents potential beneficiaries from entering the scheme as soon as they have fulfilled all entry requirements. This again does not support the achievement of sustainable development and good governance goals[38].

[34] To be presented to the Council and EP in parallel with a proposal regarding a revised scheme.
[35] For the summary of the conclusions see Annex 1 Table 1-7.
[36] See e.g., CARIS p. 180.
[37] See further explanations in Annex 1.
[38] This issue was raised by a number of stakeholders in the consultation process.

Fourth, as shown by the consultation process, one of the most debated issues is the number and nature of GSP+ conventions. The CARIS study found that the current GSP+ requirements in relation to international conventions generally support core sustainable development and good governance principles and that there is no clear-cut case for substantially reforming the list of conventions[39]. However, the list of conventions was drawn up in 2005 and should be reviewed to ensure that it is up-to-date and relevant.

Suboptimal monitoring mechanism for implementation of the conventions

Under the current scheme the Commission reviews the status of ratification and effective implementation of the conventions by examining available information from the relevant monitoring bodies. This approach has several limitations.

First, there is no generally accepted definition and interpretation of the term 'effective implementation', which creates problems for the Commission to conduct the monitoring.

Second, two conventions do not have monitoring mechanisms[40]. The *Convention on the Prevention and Punishment of the Crime of Genocide* does not provide for the setting up of a committee to monitor its implementation. The *International Convention on the Suppression and Punishment of the Crime of Apartheid* foresees the establishment of a body in charge of monitoring, but it has not been established. Thus, in practice without official monitoring mechanisms it is difficult for the Commission to carry out monitoring of effective implementation of the conventions

Furthermore, states that have signed up to the conventions are obliged to report only periodically to the monitoring committees established under each Convention. The reporting periods differ significantly (from one year up to five years). Thus, in certain cases monitoring reports are few and far between, and do not allow for prompt identification of a failure to observe the relevant conventions.

Suboptimal mechanism for withdrawal of preferences

Operational experience of the scheme has uncovered several shortcomings in its legal framework. First, the current GSP Regulation contains no clear and detailed procedural rules concerning data protection and rights of defence in the Commission's administrative proceedings. Second, the investigation procedure is unclear and lacks a precise timeline for the different procedural steps. Third, the Regulation does not contain a procedure for re-instatement of preferences.

2.3.6. Inadequate safeguard mechanism

The scheme’s safeguard mechanism has never been used in practice. This may be linked with the complaints expressed by several stakeholders in the consultation process. They have pointed out that the safeguard mechanism should be more stable and predictable. Accordingly the procedural arrangements of the safeguard mechanism were reviewed and several limitations were identified. First, the definition of key legal concepts is unclear, for example the notion of 'serious difficulty', which is the trigger for action. Contrary to other safeguard instruments, where the trigger concepts are clearly outlined, EU producers are not in a position to know what conditions are necessary for obtaining safeguards—an obstacle for their use. Second, the rights and obligations of parties in the context of the opening of investigations and of their participation in the process are not defined. This implies not only

[39] See e.g., CARIS p. 186.
[40] For monitoring bodies and respective reporting periods see Annex 1 Table 1-6.

that parties are not sufficiently aware of what triggers an investigation, but how this is done—another obstacle to the potential use of safeguards. Third, the procedural framework is also very general, and needs more detailed rules so as to enhance transparency and predictability. Otherwise, parties know neither how/when their input is required, nor how/when they can exercise their rights. As substantive and procedural question marks accumulate, it is not hard to understand why safeguards have never been used. A simple look at the degree of substantive and procedural detail present in other safeguard instruments[41] as compared to the scheme's safeguards is rather telling of the shortcomings at hand.

These shortcomings can impinge on the efficiency of safeguards, which, as confirmed by the consultation process, are an important mechanism for defending the economic and financial interests of the European Union.

2.4. EU competence in this field

The legal basis for Community action in the area is Article 207 of the Treaty on the Functioning of the European Union (hereinafter TFEU) which states that the European Parliament and the Council, acting by means of regulations in accordance with the ordinary legislative procedure, shall adopt measures defining the framework for implementing the common commercial policy.

The principle of subsidiarity does not apply in this case. The principle of proportionality is satisfied inasmuch as the regulation is the only appropriate type of action that the European Union can take to establish unilateral, non-reciprocal, preferential market access for developing countries.

3. OBJECTIVES

3.1. General objectives

The scheme has three general objectives:

1. To contribute to poverty eradication by expanding exports from countries most in need (G-1);
2. To promote sustainable development and good governance (G-2);
3. To ensure a better safeguard for the EU's financial and economic interests (G-3).

3.2. Specific and operational objectives

For the period from 2006 to 2015 the Commission GSP Communication established the following objectives for the scheme:

1. To maintain generous tariff preferences that continue to provide real incentives for developing countries to expand their exports in a sustainable manner;
2. To target the preference on the countries that most need it, in particular by terminating preferential access for countries that no longer need it, and by ensuring that GSP preferential rates are withdrawn from competitive products;
3. To offer a simple, predictable and easily accessible preference scheme ;
4. To further encourage sustainable development and good governance;
5. To provide withdrawal mechanisms and safeguard instruments in order to ensure that the sustainable development and good governance aspects of the GSP as well as the EU's financial and economic interests are protected.

[41] For example, see Council Regulation (EC) 625/2009 and its detail as to terms and conditions of imports necessary to trigger safeguards, definition of what "serious injury" means, details regarding causation aspects of the investigation, details regarding which parties can participate when, rights of defence, procedures and deadlines.

In order to ensure that policy options considered are the most appropriate for reaching the scheme's general objectives in a changing global economic environment, these objectives have been translated into specific and operational objectives:

The specific objectives are as follows:

1. To better focus the preferences on the countries most in need (S-1);
2. To remove disincentives for diversification for countries most in need (S-2);
3. To enhance consistency with overall trade objectives, whether bilateral or multilateral (S-3);
4. To strengthen the support for sustainable development and good governance (S-4);
5. To improve the efficiency of safeguard mechanisms ensuring that the EU's financial and economic interests are protected (S-5);
6. To enhance legal certainty, stability and predictability of the scheme (S-6).

The operational objectives are as follows:

1. To revise the beneficiary country list by deferring benefits to those countries, which based on their development, financial and trade needs, no longer need the preferences;
2. To target graduation on the prime beneficiaries ensuring that GSP preferential rates are withdrawn from competitive products;
3. To redefine product sections to reflect more homogeneous product categories;
4. To simplify GSP+ entry mechanism;
5. To develop a more effective and transparent mechanism for monitoring and evaluating the GSP+ countries' commitment and progress in the implementation of GSP+ conventions;
6. To develop credible and efficient procedures for temporary withdrawal of the preferences and procedures for renewal of the preferences;
7. To improve the administrative procedures of safeguard mechanisms.

4. POLICY OPTIONS

Given the complexity of the scheme and the possible changes that can be envisaged, the number of potential policy options to be analysed run in the hundreds. In view of the problems at hand, the following core policy options have been identified as being representative of the main avenues that can be selected. Annex 5 provides more details regarding this choice.

A summary table of the options is as follows:

Option	**Main features**
Option A: Discontinuation	Preferences are abandoned for GSP and GSP+ beneficiaries. EBA arrangement would remain.
Option B: No policy change **BASELINE**	The current policy continues without change. This option has two baseline scenarios: <u>B1</u> (short run) – the continuation of the scheme taking into account the current status of multilateral and bilateral agreements. <u>B2</u> (long run) – the continuation of the scheme based on the assumption

	that all on-going multilateral and bilateral negotiations have been concluded successfully.
Option C: Partial redesign	This comprises two sub-options. They have certain common elements, and certain differences—C1's changes being less extensive than C2's. **Elements common to the 2 sub-options:** 1. Preferences are deferred for certain eligible countries: • overseas countries and territories; • high and upper middle income countries; • countries with a preferential trade agreement covering substantially all preferences. 2. Graduation principles are revised: • product sections are redefined; • graduation does not apply to GSP+ countries. 3. GSP+ entry mechanism is simplified and made more flexible: • countries must only ratify, not fully implement, conventions, while committing to ensure their implementation; • countries can apply for GSP+ at any time. 4. GSP+ monitoring mechanism is redesigned to enhance implementation of the conventions. 5. More transparent and efficient procedures for temporary withdrawal of preferences are introduced. 6. The administrative procedures of safeguard mechanisms are improved. **Elements that differ between the 2 sub-options:** 1. Graduation threshold <u>Option C1</u> • Graduation threshold remains unchanged. <u>Option C2</u> • Graduation threshold is reduced to 7.5% and 50% safety net is eliminated. 2. GSP+ vulnerability criteria <u>Option C1</u> • The import-share threshold is relaxed (increased from 1% to 2%). <u>Option C2</u> • Vulnerability criteria are eliminated. 3. List of GSP+ conventions <u>Option C1</u> • The list of GSP+ conventions remains unchanged. <u>Option C2</u> • The list of GSP+ conventions is expanded.
Option D: Full redesign	This option includes and builds upon the features of option C. In particular, the product coverage of the scheme is redesigned, with 3 sub-options:

	Option D1 All beneficiary countries receive full product coverage and all products are deemed non-sensitive. No graduation takes place. Option D2 A number of industrial and agricultural products move from the sensitive to the non-sensitive list. Option D3 The list of products covered by the scheme is expanded to include a number of industrial and agricultural products.

4.1. Policy Option A: Discontinuation of the scheme

Preferences would be abandoned for GSP and GSP+ beneficiaries. Their imports would typically be subject to the standard 'most favoured nation' (MFN) conditions. If other more favourable conditions exist (*via* a bilateral agreement or another autonomous measure such as the EPA Regulation), these would apply[42].

4.2. Policy Option B: No policy change

Option B is the continuation of the current policy without any change, i.e. without any new or additional EU intervention. It is the baseline scenario against which the other policy options will be compared.

However, other elements, key to the effectiveness of the GSP but outside the remit of the GSP scheme, may change. In particular, this includes the status and likely development of multilateral and bilateral negotiations. Options A, C and D will therefore be compared against two baseline scenarios: one retaining the current status of multilateral and bilateral agreements (B1); and another where all on-going multilateral and bilateral negotiations have led to fruition (B2). B1 corresponds to the "short run", while B2 corresponds to the "long run".

4.3. Policy Option C: Partial redesign of the scheme

The main thrust of this option would be to refine the beneficiary list, graduation rules, GSP+ related procedures and criteria, and safeguards, in order to better meet the specified objectives. In order to fully capture all the main possibilities at hand, particularly regarding graduation and GSP+ criteria, option C has been subdivided into two sub-options, C1 and C2. Both share a number of elements.

Elements common to options C1 and C2

1. Deferral of preferences for eligible countries less in need[43]

To better focus preferences on the countries most in need and to remove disincentives for diversification, the preferences for a number of beneficiaries would be deferred. These would be (1) overseas countries and territories; (2) richer countries, identified on the basis of the

[42] EBA arrangements, which are not subject to periodic review and thereby outside the scope of this revision , would remain.

[43] Countries 'less in need' are those which are not 'most in need' as defined above.

World Bank classification (high income countries[44] and upper middle income countries); and countries with a preferential trade agreement which covers substantially all preferences provided under the scheme. A comprehensive table with these countries is provided in Annex 6 Table 6-1.

These countries would however remain eligible and receive preferences should their situation vary over time. This situation would be assessed regularly and beneficiary countries would be reclassified as appropriate.

2. Graduation - principles

To better focus the preferences on the countries most in need, the graduation mechanism would be revised in two ways. First, the current 21 product sections would be split into 32 subsections (see Annex 6 Table 6-2). This would ensure that product categories are more homogeneous, and consequently that graduation becomes better targeted. Second, GSP+ beneficiaries would not be graduated, as they are in general no less vulnerable than LDCs, which can not be graduated under EBA. While this may affect certain sectors within certain LDCs (as GSP+ competition would increase), this option must be examined as it provides powerful incentives for countries to join GSP+ and thus to progress in the achievement of human rights, labour rights, and sustainable development.

3. GSP+ eligibility - principles

To strengthen the support given to sustainable development and good governance the GSP+ entry mechanism would be simplified and made more flexible.

First, the condition for eligibility to GSP+ would be redefined: a country must ratify, not fully implement, the conventions, while committing to ensure their implementation. As discussed in Annex 1, to require implementation before entry is at odds with the logic of the instrument. If a country has already achieved sufficient implementation, it will tend to have overcome already the most significant political and economic hurdles associated with more stringent labour, human, and sustainable development thresholds. Thus, preferences will not add significant value. On the other hand, preferences can provide powerful incentives to those who have advanced in implementation but have not yet reached optimum levels. Put graphically, the value of the instrument is much more significant if it supports countries which are already moving up the hill and helps them in their efforts to reach the summit, rather than rewarding those who are already at the top[45].

The foregoing should not be confused with a “blank cheque” for countries to obtain benefits. Countries will not be allowed to enter the scheme on flimsy intentions, but on the basis of a firm, binding commitment which guarantees implementation of the conventions. Should these official undertakings be breached, a country would be swiftly removed from preferences—to the detriment of the many exporters which would have signed contracts with EU traders. In other words, the instrument generates powerful incentives for central stakeholders to support the often costly improvement in implementation of conventions. This is the very engine that progressively pushes countries to ameliorate human rights, labour rights, and to adopt more sustainable development strategies.

[44] As highlighted in chapter 2, high income countries are eligible under the current scheme when they are not 'sufficiently diversified'.

[45] More generally, this discussion should be set against a background where not all EU Member States have the same degree of implementation for all conventions.

Second, countries would be allowed to apply for GSP+ at any time, rather than only during limited time windows.

4. GSP+ monitoring mechanism

To further strengthen the support for sustainable development and good governance by ensuring the effective implementation of GSP+ conventions, a more effective and transparent mechanism for monitoring and evaluating the implementation of GSP+ conventions would be developed.

This would shift the onus of proof that conventions are being implemented from the EU institutions to the beneficiary country. This effectively raises the requirements for beneficiary countries, as they have to positively prove that implementation has indeed taken place – rather than (at present) obliging EU institutions to prove that identified shortcomings have not been remedied.

Also, the monitoring procedure would be formalised, with the current GSP+ dialogue being incorporated into the Regulation. This dialogue would be based not only on the evidence emanating from monitoring bodies, but also on the information provided by other sources, including Council and the EP. This would enrich the basis for assessment, as the additional sources would complement with more current information the conclusions of monitoring bodies, which are not always updated every year.

Furthermore, the results of this monitoring would be presented more regularly to Council and the EP.

Together, these elements should make the monitoring system substantially more accurate and comprehensive.

5. Mechanism for withdrawal of preferences

To strengthen the support to sustainable development and good governance and to enhance legal certainty, stability and predictability, credible and efficient procedures for temporary withdrawal of preferences would be developed, including rules concerning confidentiality and rights of parties; and a withdrawal procedure with a clear timeline for the different procedural steps, would be introduced. The procedures for renewal of the preferences would also be developed.

6. Safeguard mechanism

Equally, to ensure a better safeguarding of the EU's financial and economic interests and to enhance legal certainty, stability and predictability, the administrative procedures for safeguard mechanisms would be improved by developing clear definitions of key legal concepts, by specifying the rights of parties during the investigation and by elaborating clearer administrative procedures.

Elements that differ between options C1 and C2

1. Graduation - thresholds

To further improve the focusing of preferences on those most in need, it is important that all competitive sectors are graduated. Two possibilities for fixing the appropriate thresholds are explored. C1 maintains the current procedures as described in Annex 1. This approach is based on the fact that, as preferences for a number of current beneficiaries are deferred, the calculation of thresholds is performed on a smaller pool of imports. Thus, without changing the threshold, graduation would naturally tend to weed out the more competitive product sections.

In addition to a smaller pool of imports, C2 reduces the thresholds by half to 7.5%[46], and eliminates the 'safety net' 50% threshold described in Annex 1. This means that in practice graduation becomes much more stringent, and many more product sections are identified as competitive.

Thus, C1 and C2 allow for a more comprehensive assessment of the graduation spectrum.

2. GSP+ eligibility - thresholds

To strengthen the support for sustainable development and good governance provided by the GSP+, there are a number of possible ways to make the system more open to potential beneficiaries. Two sub-options are explored. C1 is the less extensive approach of the two. It relaxes the existing vulnerability criteria by increasing the import-share threshold from 1% to 2%, while the diversification criterion remains stable (at 75%, based upon the preponderance of exports accounted for by (roughly) the 25% highest exporting product sections[47]). Also, the list of GSP+ conventions would remain unchanged.

C2 is more extensive. It does away with vulnerability criteria altogether. Equally, the list of conventions is revised by (1) removing conventions that do not have monitoring mechanisms and by (2) requiring additional commitments on relevant conventions (e.g., recent protocols relating to the implementation of existing GSP+ conventions, or additional protocols to human rights conventions, or completely new conventions on the environment, maritime and fisheries governance[48]).

Thus, C1 and C2 allow for a more comprehensive assessment of the GSP+ eligibility spectrum.

4.4. Policy Option D: Full redesign of the scheme

This policy option includes and builds upon the features of option C and offers further redesign of the scheme by revising GSP 'product coverage'—the only building block of the scheme not included in option C.

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[46] 7.5% emanates from the CARIS report, which highlights that graduation would become a much more powerful tool as of that level.

[47] In the current system of 21 sections, diversification is based on the export performance of the 5 largest sections (i.e., slightly less than 25%). If we were to increase the product categories to 32 sections, we would need to consider the performance of the 7 or 8 largest sections in order to keep the proportion constant. For the purpose of this document, 8 sections are considered. As with othet sections of this Impact Asesssment, this does not prejudge an eventual Commission proposal as to the number of sections.

[48] Salient items are the United Nations Convention on the Law of the Sea of 10 December 1982 (UNCLOS); the Agreement for the implementation of the provisions of the Convention of 10 December 1982 relating to the conservation and management of straddling fish stocks and highly migratory fish stocks of 4 August 1995 (UNFSA); the FAO Agreement to Promote Compliance with International Conservation and Management Measures by Fishing Vessels on the High Seas of 24 November 1993 (FAO Compliance Agreement); Additional Protocols I and II to the Geneva Conventions, Second Optional Protocol to the ICCPR, the Optional Protocol to the Convention against Torture and the two Optional Protocols to the Convention on the Rights of the Child on the involvement of children in armed conflict and on the sale of children, child prostitution and child pornography.

This can be done in two ways: (1) more products can be subject to the scheme; (2) sensitive products can be reclassified as non-sensitive. As regards (2), this 'desensitisation' means that duties would be set at 0% for all beneficiaries. This would remove the preference (bias) that GSP+ and LDC beneficiaries have currently towards particular products, that arises because they enjoy 0% duties on such products while GSP beneficiaries pay positive duties.

To explore the full spectrum of possibilities, 3 sub-options are identified, one more far-reaching, and two intermediate ones.

Sub-option D1 implies full product coverage and full desensitisation. In other words the equivalent of duty-free, quota-free treatment currently enjoyed by LDCs is provided to all beneficiaries. This treatment implies that graduation would not take place. While far-reaching, this option reflects the views of certain stakeholders regarding the scheme.

Sub-option D2: partial desensitisation, but no expansion of products subject to the scheme. In order for desensitisation to be meaningful in terms of additional preferences, it must include a significant number of sensitive lines, with significant preferences.

For non-agricultural products, all sensitive products for which MFN tariffs are equal to or lower than 3.5%[49] have been selected[50]. This amounts to roughly 300 lines (or over 10% of the total).

Agricultural goods have a much broader base than industrial goods in the beneficiary countries. In order to arrive at a meaningful set of products, we have identified from the subset of products currently considered as "sensitive", those goods of key interest for the countries involved. These include fish and their preparations, vegetable oils, fruits and their preparations and juices, vegetables and their preparations, nuts, tobacco, pasta, and processed cereals[51].

Sub-option D3: no desensitisation, but partial expansion of products subject to the scheme. As regards non-agricultural products, only a very few (about 130) tariff lines (see Annex 4, Table 4-4) are not subject to the scheme. In order to have a meaningful expansion, roughly 100 tariff lines have been taken (basically, all lines except arms and nuclear materials). The expanded lines include mainly chemicals, textiles, and raw materials[52].

From the subset of agricultural goods products currently outside of scheme, a list of agricultural exports of key interest for beneficiary countries has been identified. This includes wheat, rice, maize, molasses prepared meat and ethanol[53].

5. ANALYSIS OF IMPACTS

5.1. General

Imports benefiting from preferences account for less than 5% of total EU imports. This implies that, while impacts on beneficiaries may be large, the general impacts on the EU are

[49] 3.5% is taken as a yardstick for significance in preference levels as the current rules apply a 3.5% reduction in duties for GSP beneficiaries' imports of sensitive products—a reduction which is considered significant.
[50] See Table 6-15.
[51] See Table 6-15.
[52] See Table 6-16.
[53] See Table 6-16.

likely to be of a limited nature. Where impacts are considered to be insignificant, the principle of proportionality of assessment is applied, as per the Impact Assessment Guidelines.

Impacts have been assessed using a number of tools, which include CARIS modelling, additional analysis via a SMART model, and the examination of official EU imports, production, consumption and employment statistics. More information on these models and their limitations is presented in Annex 6.3.

It is also underlined that the main variable used to analyse social impacts has been employment.

5.2. Comments on the baselines (B1 and B2)

There is a natural reduction in the level of import duties (and, therefore, preferences) as more bilateral agreements and a multilateral agreement come into force. This phenomenon is called 'preference erosion'. This dynamic impact is shown as analysis move from the baseline corresponding to the present (B1) to the baseline where all on-going (but unfinished) negotiations have entered into force (B2).

Preference erosion reduces imports from beneficiaries. B1 incorporates the negative effects of the newly concluded agreements such as those with South Korea and certain Latin American countries (see Annex 6.4 Table 6-4). The negative impacts would be much larger in B2, where the multilateral trade round known as the DDA and the rest of on-going bilateral negotiations would have been concluded (see Annex 6.4 Table 6-6).

This is the reality against which this assessment takes place: preferences will drop significantly (or even disappear). In the long run, when all multilateral and bilateral agreements are fully implemented, duties are likely to be so low that the idea of *preferences* themselves becomes largely irrelevant—and so would a generalised system of *preferences*[54]. Other totally different tools may have to be designed[55].

Until then, the question is what can be done for the countries most in need of preferences—against the backdrop of the significant competitive pressure exerted on these countries by the more advanced beneficiaries of the current scheme.

Impacts are assessed against the baselines. A detailed assessment starts with a comparison with B1 and then extends the analysis to B2[56].
For the ease of reference in the analysis that follows, tables 6-4 and 6-5 from Annex 6.4 are reproduced here:

Reproduction of Table 6-4. Summary of simulated effects of the B1 (short-run) baseline and the options (€ million*)

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[54] This is depicted numerically in Annex 6.4, Table 6-7. In the long run, the only options that would help countries most in need (C1, C2, D2 and D3—see analysis below) all yield negative results. The message is that preferences are so low that the system itself ceases to be meaningful.

[55] Such as the idea of 'negative duties' which actually is a very different concept. While preferences are revenue forgone linked to import tariffs, "negative duties" are disbursements from the EU budget which are not linked to tariffs—falling squarely into the category of "aid". This would have to be examined in a totally different framework—not under GSP.

[56] See Annex 6.1 for comparison of all beneficiary countries under each of the options and sub-options. This depicts which countries would be beneficiaries from which scheme under each option, and which exports (product category and percentage) would be graduated for which country.

Short-run baseline	Trade creation [a]	Trade diversion [b]	Consumer Surplus [c]	Change in EU tariff revenue [d]
Initialled and recently concluded FTAs	2235	-1608	1669	-1594
GSP Options				
A. Removal of the GSP (except the EBA)	-6269	4326	-3612	3510
B. Status quo				
C1. Removing high- and upper middle income countries, Graduation, sections split, threshold 15%, Pakistan, Philippines and the Ukraine to GSP+[57]	-3649	2078	-1774	1694
C2. Removing high- and upper middle income countries, Graduation, sections split, threshold 7.5%, Namibia, Nigeria, Pakistan, Philippines and the Ukraine to GSP+[58]	-4056	2381	-2015	1929
D1. DFQF for remaining GSP beneficiaries	14796	-8328	12290	-11870
D2. "Desensitisation" of certain products	-3923	2267	-1918	1830
D3. Product scope expansion	-3953	2293	-1932	1827

Source: Own calculations. * Figures converted from $US into € using an exchange rate of $1.30 per €.

[a] Trade creation refers to the direct effects (positive or negative) on a country that is subject to GSP trade policy reform (e.g. graduation, inclusion in GSP+, etc).
[b] Trade diversion captures the indirect trade impact (positive or negative) on third countries (either part of GSP/GSP+/LDC or not) as a result of the change in GSP status of any given country. Unlike a simple FTA formation, given the complex nature of GSP reform, trade diversion is therefore a composite net measure of both positive and negative trade effects on both GSP beneficiaries and third countries in the rest of the world.
[c] Consumer surplus is a main component in welfare effects and captures essentially the benefits consumers derive from being able to buy products at a price lower than what they would otherwise be prepared to pay. Trade liberalization leads to positive changes in consumer surplus.
[d] Changes in tariff revenues reflect the combined effect of changes in tariffs and changes in trade flows before and after each GSP reform scenario.
For a more formal description of all these effects and the way in which they are derived in the SMART model, see explanation above.

[57] A bilateral agreement is being negotiated with the Ukraine. As with other bilateral agreements, this would provide significantly larger market access for Ukraine than the scheme.
[58] Bilateral agreements are being negotiated with Nigeria and Namibia. As with other bilateral agreements, this would provide significantly larger market access for thee countries than the scheme.

Reproduction of Table 6-5. Summary of simulated effects of the B1 (short-run) baseline per country group (€ x 1.000)

Country group	**Option A**	**Option C1**	**Option C2**	**Option D1**	**Option D2**	**Option D3**
EBA	125.597	-4.597	16.994	-756.710	10.038	13.223
GSP+	-	999.435	1.008.599	-309.693	1.040.624	1.058.609
GSP	-	-970.175	-1.599.605	22.297.949	- 1.444.858	- 1.536.673
Total Scheme	***125.597***	***24.663***	***-574.012***	***21.231.545***	**-394.197**	**-464.841**
ExGSP[59]	- 8.591.432	- 5.027.345	-4.956.183	-2.090.720	- 4.990.947	- 4.997.790
RW[60]	2.197.327	1.354.043	1.473.832	-4.344.808	1.461.376	1.509.160
Total	**- 6.268.509**	**- 3.648.639**	**-4.056.362**	**14.796.018**	**- 3.923.767**	**- 3.953.471**

5.3. Option A: discontinuation

Option A ends the GSP scheme while retaining the EBA scheme which benefits LDCs.

Effect on EU imports: trade creation and diversion

Relative to baseline B1, total EU imports would not vary to a significant extent (the drop would be in the order of €6 billion, less than 1%[61]).This is not surprising given the low relative weight of the scheme's imports (see section 5.1 above).

However, GSP and GSP+ beneficiaries would lose, as indicated by the SMART model (see Annex 6.4 Table 6-5). Their loss is in the order of €9 billion imports—or around 20% of their current preferential imports. While the figures are only intended to provide orders of magnitude, the effect would clearly be large. In addition, this loss would affect indiscriminately all beneficiaries regardless of their needs. In particular, the countries most in need such as GSP+ beneficiaries and poorer GSP countries would be affected.

Exports from other non-GSP countries would increase by roughly €2 billion and from LDCs, by more than €100 million. Even though it only indicates an order of magnitude, the latter figure may appear small. Yet it is of crucial importance. Indeed, the effects of preference erosion are reduced, rather than worsening in line with the current trend. In addition, as explained in Annex 6.3, the SMART analysis captures only the static effects of changes in duties. It is expected that the dynamic effects will be important. As increasing opportunities arise given the deferral of preferences for key competitors, exports by LDCs will tend to increase significantly[62].

59 Former GSP beneficiaries

60 Rest of the world

61. Net change in EU imports of over €6 bn (see Annex 6.4 Table 6-5) divided by total imports of over €1.1 trillion (Annex 1, Table 1-3).

62 Empirical corroboration is provided by looking at past import trends in Annex 4 Table 4-8. Even in a context of preference erosion, LDC preferential exports increased significantly since 2005. Without this preference erosion, the increase should not only continue, but be higher.

Unsurprisingly, the scale of effects under option A would roughly halve on the hypothesis that all on-going negotiations have come into force (B2), given the considerable reduction of duty levels—and thus available preferences.

Effects on welfare, including EU consumer surplus
Assessment starts with analysis of the effects as compared to baseline B1.

For former GSP and GSP+ beneficiaries, the approximate welfare effects of this option can be obtained from CARIS[63]. Unsurprisingly, most of these are negative. Moderate negative impacts (below -0.10%) are recorded for many countries, the most salient of which are Latin American GSP+ countries, Brazil, Pakistan, Thailand, Russia and Ukraine. Significant impacts (below -0.25%) are recorded for countries such as Ecuador, Argentina and the North African rim.

Perhaps more surprising are the very low or negligible impacts on countries such as India, Brazil, and the Philippines. This underlines that for many GSP beneficiaries, preferential exports to the EU are not economically significant for the country as a whole. For EBA countries, the welfare effects are expected to be in line with the increase in imports: positive, but not very significant. Unsurprisingly, the welfare of the rest of the world (approximated by the category 'rest of OECD') barely changes.

Also unsurprisingly, the impact on EU welfare is negligible (0.02%). Changes in consumer welfare are not provided by CARIS, but an order of magnitude can be obtained from the SMART analysis. The consumer surplus drops by less than €4 billion, or less than 0.05% of the EU's GDP[64]—again a very low figure.

Relative to baseline B2, the impacts (both positive and negative) will be much lower given than the changes in imports are roughly half of those under B1.

Effects on production and employment: sectoral impacts
For this section, the analysis is limited to the countries within the scheme and to the EU, based on CARIS. Impacts on production will be considered significant if they are equal to or exceed 1%; and on employment if they are equal to or exceed 0.5%[65].

The approximate effects of option A (relative to B1) are depicted in Annex 6.5 where significant positive and negative sectoral impacts are highlighted for output (Table 6-8), unskilled labour (Table 6-10), and skilled labour (Table 6-11). Given the large number of countries involved, the impacts vary. However, sectoral impacts are both positive and negative for most countries, so that, on the whole, they tend to compensate each other. The areas where net impacts may be negative due to the importance of certain sectors and/or the size of variations are Ecuador (fruits and vegetables), Pakistan (apparel), Argentina (oils and fats), the North African rim (oils and fats, textile and apparel, leather products) and South Africa (rice).

Within the EU, production and employment effects would on the whole not be significant. However, certain sectors would clearly benefit: the sugar sector, with almost a 4% increase,

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[63] See Annex 4 Table 4-9. The relevant column would be MFN04, which removes all preferences for <u>all</u> developing countries (including LDCs).
[64] €11.8 trillion in 2009 at current prices, according to official statistics.
[65] These thresholds are also used to assess changes in production and employment for all other options.

and fruits and vegetables, textiles and apparels (each in the 0.5% range). Given the high level of employment in the latter sector (7,8% of all EU manufacturing jobs—see Annex 6.6, these effects can be rather positive for countries such as, Estonia, Greece, Hungary, Italy, Latvia, Lithuania, Malta, Poland, Spain, Slovenia and Slovakia, where the sector is particularly important.

Relative to baseline B2, the impacts of option A (both positive and negative) will be much lower given that the changes in imports are roughly half those occurring under B1.

Effects on EU tariff revenue[66]

When compared to baseline B1, the combined impact of GSP and GSP+ exports becoming subject to higher duties, and the increased exports from third countries already subject to duties, imply that tariff revenue would increase, as indicated by the SMART analysis (see Annex 6.4, Table 6-4)[67]. The increase is in the order of €3 to €4 billion, which would add to current tariff revenues of roughly €19 billion (see Annex 7, indent 17 for details)[68]. The impact when compared to B2 would unsurprisingly be smaller—an increase of under €2 billion[69].

Effects on on-going trade negotiations

As explained before, these effects are irrelevant, as the scheme can not be defined on the basis of anything other than the trade, financial and development needs of beneficiaries. Nevertheless many GSP and GSP+ beneficiaries are in the process of negotiating bilateral agreements with the EU, and a vast majority are WTO members. The unintended consequence of removing autonomous preferences under the scheme would be to provide an additional incentive to pursue these negotiations.

Regarding the specific issue of EPAs, changes in the scheme are bound to have a rather limited impact on the negotiation dynamics. There are two reasons for this. The first is that EPAs are far superior to GSP as a mechanism to ensure preferential access to the EU. EPAs are a permanent, enforceable instrument, rather than an autonomous measure which can be withdrawn at will by the EU. EPAs are comprehensive in terms of product coverage for all partners. And they also offer flanking measures to aid development.

The second reason is the existence of other ways to enjoy access to the EU market independent of the scheme. Only 8 partners out of 74[70] countries which negotiate EPAs do not benefit either from EBA treatment or from the benefits of the EPA Market Access Regulation—which provides extensive preferences. In the highly unlikely event of knock-on effects on EPAs, these would be concentrated in the aforementioned 8 countries.

Effects on the environment

The effects of international trade and economic development on the environment are widely discussed. According to standard analysis[71], trade has at least four types of impacts on the

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[66] The effects on the EU budget will be assessed on the basis of tariff revenue throughout this document.

[67] Only direct effects on the budget are used for the purpose of our analysis throughout this text.

[68] This does not take into account the impact of the trade agreements which have been initialled and are coming into force. If this were the case, the €19 billion figure would drop by around €1.5 billion.

[69] This does not take into account the impact of the conclusion of the multilateral round of negotiations, plus all the other on-going bilateral negotiations. If this were the case, the €19 billion figure would drop by around €14 billion.

[70] Cook Island, Gabon, Marshall Islands, Micronesia, Nauru, Nigeria, Democratic Republic of Congo, Tonga.

[71] See in particular *The Environmental Effects of Trade*, Paris: OECD, 1994.

environment: i) *product effects* (i.e. traded products themselves have a – positive or negative – impact on the environment); ii) *scale effects* (i.e. trade expands the level of economic activity, possibly – but not necessarily – increasing economic efficiency); iii) *structural effects* (i.e. trade changes the composition of a country's economy, which may again have both positive and/or negative environmental impacts) and iv) *direct effects* (i.e. environmental impacts caused by trade per se, for instance transport). The empirical results of the studies having examined the trade-environment relationship in the last few years are mixed. While some studies show that trade liberalization reduces pollution, others have concluded that trade liberalization has had a negative impact on the sustainable development of various developing countries. For the purpose of assessing possible impact of the scheme, the following studies in particular have been referred to: the CARIS study and the Special Study on Trade and Environment[72]. We focus on direct effects for the purpose of this analysis. Indeed, these are considered the most salient against a backdrop of modest trade volume changes—and thus not very significant product, scale or structural effects[73].

The likely impact of the scheme on environment, both within the EU and in the beneficiary countries, will be directly proportional to its relative share in the overall trade flows, and will also be linked to the geographical distribution of import sources. In this respect, it is important to note that the share of preferential imports represents less than 5% of total EU imports. Therefore, it is unlikely that the scheme itself has any *direct effect* on the environment.

When compared against B1, option A confirms the foregoing. With an impact on trade of less than 1%, this option would not appear to have a significant impact on the environment. The positive effects on the environment of marginally lower trade would tend to be compensated i.a. by other negative effects—such as those linked to the loss of support for environmentally sustainable development via GSP+.

These limited impacts would tend to further decrease under B2—were import volumes vary even less.

Other effects

Regarding administrative costs[74], the drop in overall import volumes is marginal, so any gains would not be significant. These gains would also have to be balanced against potentially higher costs linked to collection of higher tariff revenues. On balance, no significant variations are expected.

Regarding safeguards, the same mechanisms as today would apply, with the same efficiency gaps.

[72] Trade and Environment by Håkan Nordström and Scott Vaughan http://www.wto.org/english/res_e/booksp_e/special_study_4_e.pdf.

[73] Reference is made to the principle of proportionality of assessment.

[74] It is recalled that changes in preferential rules of origin are not analysed in this impact assessment. The only salient administrative costs generated by the scheme are precisely costs related to preferential rules of origin. (Given the simplification of the new rules which entered into force in January 2011, these costs are expected to decrease in the medium term, after the typical short-term adaptation costs.) For completeness sake, we have analysed other residual administrative costs linked to changes in the volumes of trade and customs duties.

General assessment of economic[75], social and environmental effects

Relative to B1, the general effects are as follows. The economic and social effects on countries most in need are expected to be negative. LDCs will benefit, but the many other countries and economic sectors which are also most in need will suffer as preferential access disappears.

Within the EU, three elements will impact upon general economic and social effects: producer surplus, consumer surplus, and tariff income. Negative impacts for consumers are likely to be compensated by higher tariff revenues, which are of the same order of magnitude. The net impact would thus be generated by benefits to producers. As explained above, these benefits would on the whole not be significant, but would have significant positive effects on important sectors—and on those EU Member States where these sectors are important. Therefore, these impacts would be positive as a whole.

Environmental impacts in the EU would be (at best) marginally positive, given that the drop of imports would be marginal. As for the countries most in need, it is possible that those countries losing GSP+ would deviate from environmentally sustainable practices. Thus, on the whole, a marginally negative impact would be felt.

A vs. B1. Effects on:	**economic**	**social**	**environmental**
Countries most in need*	--	--	0/-
EU	+	+	0/+

*Negative economic and social impacts for countries most in need *as a whole* hide positive impacts on LDCs.

Relative to baseline B2, the changes would be expected to go in the same direction, but they would be significantly smaller—to the point of not being noticeable.

5.4. Option C: partial redesign

Option C has many building blocks. To explore the different angles of these building blocks, two sub-options were explored. The main differences between them concern the graduation of competitive sectors and the vulnerability criteria under GSP+.

With regard to graduation, the sectors which will actually be graduated are not known at this stage. They will depend on the calculations of imports on the basis of the latest available figures prior to the entering into force of the new Regulation[76]. Current figures have been used as a proxy. Graduation under C1 and C2 is shown in Annex 6.1 (see fist footnote of Table 6-1 for further details).

With regard to vulnerability, C1 relaxes the 'economic' criterion from 1% to 2%. The actual list of countries which will meet the relaxed criterion is not known at this stage—again, these

[75] Throughout part 5, “Economic effects” refer here to all the effects analysed with the exception of effects on employment, environment and on on-going trade negotiations. These are effects on trade, welfare (including consumer surplus), production, tariff revenue, administration costs and those linked to the use of safeguards.

[76] Given the statistical time lag, these are likely to correspond to 2009, 2010, and 2011.

calculations will be made on the basis of the latest available figures[77]. Pakistan, Philippines and Ukraine have been considered as a proxy for the purpose of this exercise[78].

Also, C2 eliminates the vulnerability criteria while it adds additional requirements regarding conventions. Again, the actual list of countries meeting the relevant conventions criterion will be determined as close as possible to the time of entering into force of the new Regulation[79]. This is more subjective, as the decisions to ratify conventions and to commit to their implementation are ultimately political. The three C1 countries plus Namibia and Nigeria have been used as a proxy for the purpose of this exercise.

The assessment starts with analysis of option C1 and then describes the main differences that arise under option C2.

5.4.1. Option C1

Effect on EU imports: trade creation and diversion

Relative to base line B1, total imports would drop by about €4 billion (see Annex 6.4 Table 6-4). Again with the proviso that it merely points to an order of magnitude, this relatively low figure is made up of both an increase and a drop. Imports from countries which never belonged to the scheme rise by approximately €1 billion (see Annex 6.4 Table 6-5).At the same time, imports from countries which cease to be beneficiaries drop by around €5 billion (see Annex 6.4 Table 6-5). This drop is significant, taking into account that their preferential imports were around €21 billion in 2009.

In contrast to the situation under option A, where only LDCs benefited, the countries most in need are in a better position *as a whole*. Under SMART's static approach, the increase in import would be about €25 million (see Annex 6.4 Table 6-5). As in the case of option A, the figure may appear small, but it implies that the impacts of preference erosion are reduced not only for LDCs, but also for other countries most in need. In addition, dynamic effects will cause this figure to increase as further opportunities arise given the deferral of preferences for key competitors.[80]

The positive impact on countries most in need will be mostly concentrated on GSP+ beneficiaries, rather than LDCs. This is largely explained by the entry of Pakistan into GSP+, which depresses the textile exports of Bangladesh, the largest EBA exporter by far (see Annex 4 Table 4-8). Without Bangladesh, LDC exports would increase for option C1 (by about €20 million).

Other notable variations within the category are the increases in Ukrainian exports (+ €150 million) and Philippine exports (by more than €75 million). On the other hand, significant losses accrue to Vietnam (more than €90 million) and India (more than €450 million), on

[77] Given the statistical time lag, these are likely to correspond to 2009, 2010, and 2011.
[78] This is indicative only. For example, under a scenario of 7 sections instead of 8, Ukraine is not eligible.
[79] Given the statistical time lag, these are likely to correspond to 2009, 2010, and 2011.
[80] Empirical corroboration is provided by looking at past import trends. Even in a context of preference erosion, non-LDC countries which are most in need increased their preferential exports significantly since 2005. For such countries in the GSP category, the increase reached 20%; for GSP+ countries under C this was around 85%. Without the effects of preference erosion, the increase should not only continue, but be higher.

account of the increased competition in textiles and fish products from new GSP+ beneficiaries—and due to increased graduation of their exports.[81]

As in option A, these effects would decrease substantially (and in some cases even disappear) on the hypothesis that all on-going negotiations have come into force (B2), given the much lower level of duties—and thus of available preferences.

Effects on welfare, including EU consumer surplus
Assessment starts with the analysis of the effects as compared to baseline B1. The analysis will draw only partially from CARIS regarding this aspect, as the study does not have a scenario which mirrors the options included under C.

For former GSP and GSP+ beneficiaries, the approximate welfare effects of this option are similar to those under option A. One would expect welfare losses of the same order of magnitude as above for Brazil, Argentina, Russia, South Africa and the countries of North Africa. Other ex-beneficiaries would suffer as well.

A second category of ex-beneficiaries includes those with bilateral agreements with the EU, the conditions of which approximate or surpass the preferences offered by the Scheme[82]. For these countries, the impact should be neutral or moderately positive, as other competitors also exit the scheme.

As to the welfare of countries most in need, this should increase overall. CARIS[83] can approximate the effects for countries such as Ecuador (+2.39%), other GSP+ Latin American countries (+0.31%), Ukraine (+0.36%). For other salient countries, the increase of Pakistani or Philippine exports suggests a moderate to significant increase in welfare. For Vietnam, the drop in exports suggests a moderate to significant decrease, while for China and India, no noticeable drop should ensue[84]. For EBA countries, the welfare effects are expected to be in line with the increase in imports: positive, but not very significant. Bangladesh would be the salient exception, with a significant welfare loss, estimated at 0.31%[85]. Overall, the picture would thus be positive, in line with the general increase in exports to the EU.

Given that the increase in imports is lower than for option A, no significant impacts on the rest of the world are expected.

Unsurprisingly, the impact on EU welfare would not be noticeable. CARIS calculates a welfare loss of 0.05% even when all developing countries obtain full preferences—far beyond anything proposed under option C1. Changes in consumer welfare are not provided by CARIS, but an order of magnitude can be obtained from the SMART analysis (see Annex 6.4

[81] Again, trade would increase considerably more under a bilateral agreement (e.g. in the case of the Ukraine or India) than under the scheme.
[82] E.g., the last series of agreements with Latin American countries.
[83] See Annex 4 Table 4-9. The relevant column would be ZEROTM, which provides full preferences for all developing countries. This scenario underestimates benefits under C for countries most in need—C defers benefits for many countries that get full preferences under ZEROTM. So these figures should be understood as a "floor", with benefits being potentially much higher.
[84] See CARIS scenario MFN04. For China, even a total loss of preferences yields no change, given the fact hat most of its products are graduated in any event. For India, even a total loss of preferences would also yield no change.
[85] See CARIS scenario MFN04.

Table 6-4). The consumer surplus drops by about €2 billion, or less than 0.05% of the EU's GDP—again a very low figure.

When compared to baseline B2, the impacts of option C1 (both positive and negative) will be much lower given that the changes in imports are a third of those foreseen when comparing C1 with baseline B1. The partners which lose beneficiary status in the scheme but enter into a preferential trade agreement with the EU (e.g., Brazil, Argentina…) will regain preferential access at least as advantageous as that offered by the scheme.

Effects on production and employment: sectoral impacts

For this section, the analysis will concentrate on (1) the countries in the scheme where import and/or welfare impacts are significant[86]; and (2) on the EU. Wherever possible, the analysis will be based on CARIS.

Countries whose preferences are deferred and that do not have a bilateral agreement to secure similar access to the EU may suffer production and employment effects. Their situation would be similar to that under A—and in some cases worse as other non-LDC beneficiaries (and competitors) maintain preferential access under the scheme. Therefore, one can expect countries such as Argentina, South Africa, or those in the North African rim to suffer. It is also possible that countries such as Brazil or Russia can face noticeable problems in some sectors.

For the beneficiaries (i.e., countries most in need), results are expected to be positive, in line with welfare increases. Putting together the effects identified by CARIS[87] and the sectors in which export increases have been identified by the SMART analysis, it becomes apparent that for most beneficiaries, the number of sectors benefiting from significant positive production/employment effects outweigh by far those sectors with negative effects. Salient winners are as follows: Ecuador (fruits and vegetables), Georgia (oils and fats, sugar, apparel and textiles, chemical products), Philippines (apparels and textiles, leather, fish), Pakistan (rice, apparels and textiles, leather) and Ukraine (arable crops, sugar, apparels and textiles, leather). LDCs would also win as a group, with the exception of Bangladesh which can suffer heavily in textiles and apparel. India and Vietnam can also suffer in the textile and apparel or leather sectors.

As regards the EU, overall effects are not expected to be significant, but negative impacts on production and/or employment would exist in the rice, arable crops, oils and fats, sugar, fruit and vegetables, apparel and textiles, and leather sectors. Again, it is the latter three which have the largest weight in terms of employment—so the countries which would benefit under option A would turn out to be losers under option C1. Some of these countries (Estonia, Greece, Hungary, Italy, Latvia, Lithuania, Poland, Spain, Slovenia) have important agricultural production and would compete directly with some of the agricultural products just mentioned—so negative effects there can be significant.

When compared to baseline B2, the impacts of option C1 (both positive and negative) will be much lower given than the changes in imports are a third of those foreseen when comparing with baseline B1. Again, successful multilateral and bilateral negotiations will cause such profound impacts, that the scheme will have a limited residual influence.

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[86] Impacts on production will be considered significant when they exceed 1%; on employment when they exceed 0.5%.

[87] ZEROTM scenario, which as explained above would be the minimum benefits expected.

Effects on EU tariff revenue
When compared to baseline B1, the combined impact of exports from certain former beneficiaries becoming subject to higher duties, and the increased exports from third countries already subject to duties, imply that tariff revenue would increase, as indicated by the SMART analysis (see Annex 6.4 Table 6-4). The increase is in the order of €2 billion, which would add to current tariff revenues of around €19 billion[88]. The impact as compared to B2 would be smaller—a drop of under €1 billion[89].

Effects on on-going trade negotiations
From a substantive perspective, similar consideration as to those mentioned in relation to option A apply here. Of course, as more partners would remain as GSP beneficiaries under option C1, the potential effects of this option on on-going trade negotiations would be less important.

The remarks made under option A relating to EPAs also apply here. The effects (if any) should be rather limited. The only (marginal) nuance is the potential GSP+ membership of certain countries such as Nigeria and Namibia—but the latter already enjoys preferential treatment via the EPA market access regulation. EPA's superiority as a permanent tool virtually eliminates the possibility that implementing option C1 would affect EPA negotiation dynamics negatively. EPAs offer the sort of comprehensive access the scheme does not under this option.

Effects on the environment
Option C1, with an impact on trade of much less than 1%, would not appear to have, overall, a significant impact on the environment.

In this case, however, there would be two positive effects on the environment: those of marginally lower trade (both in the EU and in exporting countries); and those of extended GSP+ membership, with its support for environmentally sustainable development.

Whatever environmental effects are recognised when comparing option C1 with baseline B1 would become even less significant when the comparison is made with B2, given that import levels change even less.

Other effects
In respect of administrative costs[90], effects are not expected to be significant. The same three-tier system is maintained, with the associated administrative procedures. While imports under the scheme will drop, imports from other countries will increase, leaving the net reduction in imports at marginal levels. As under option A, any drop in costs linked to such lower imports will be balanced against potentially higher costs linked to collection of higher tariff revenues. On balance, no significant variations are expected.

[88] This does not take into account the impact of the trade agreements which have been initialled and are coming into force. If this were the case, the €19 billion figure would drop by around €1.5 billion.
[89] This does not take into account the impact of the conclusion of the multilateral round of negotiations, plus all the other on-going bilateral negotiations. If this were the case, the €19 billion figure would drop by around €14 billion.
[90] It is recalled that changes in preferential rules of origin are not analysed in this impact assessment.

This option includes improvements in the safeguard procedures, as well as in the procedures for GSP+ entry, monitoring and withdrawal. This should improve the efficiency and transparency of those mechanisms, providing for enhanced stability, legal certainty and predictability.

General assessment of economic, social and environmental effects
When compared with baseline B1, the general effects of options C1 are as follows. The economic and social effects on countries most in need are expected to be positive, as exports increase and welfare gains accrue.

As under option A, negative impacts on EU consumers are likely to be compensated by higher tariff revenues, which are of the same order of magnitude. The net impact would thus be generated by impacts on producers. As explained above, these benefits would on the whole not be significant, but would have significant negative effects on important sectors—and on the EU Member States where those sectors are important. Therefore, these impacts would be negative as a whole.

Environmental impacts in the EU would be (at best) marginally positive, given that the drop of imports would be marginal. As to the countries most in need, the impact of expanded GSP+ membership would lead overall to a marginally positive impact.

C1 vs. B1. Effects on:	economic	social	environmental
Countries most in need	++	++	0/+
EU	-	-	0/+

When comparing the effects of options C1 with baseline B2, the changes would be expected to go in the same direction, but they would become significantly smaller—again to the point of not being noticeable.

5.4.2. Option C2

From the point of view of impacts, there is one key difference between C2 and C1. Lower graduation thresholds increase the level of graduation significantly for certain countries and sectors, particularly for India. In addition it graduates country-sector combinations which are not known for their competitiveness. These rather bizarre “outliers” (Iran, Ivory Coast, Kenya) signal that the graduation mechanism is going beyond its intended effects to identify competitive sectors. This leads to a number of effects. The first one is a larger decrease in exports by GSP participants as a whole. The second is an increase in EBA exports, as negative impacts on Bangladesh diminish[91]. The result is that, while the positive effects on EBA and GSP+ beneficiaries can not be underestimated, GSP exports by many beneficiaries will suffer. Dynamic effects are expected to more than compensate for this static loss, so the impact as a whole is considered to be positive, but certainly less so than C1. Given that the remaining impacts (including those related to GSP+) are largely similar to C1, the only noteworthy change would thus affect the general assessment table, which would read as follows.

[91] More textile products are graduated for other beneficiaries—losing their preferences in product which compete with Bangladesh.

C2 vs. B1. Effects on:	economic	social	environmental
Countries most in need	+	+	0/+
EU	-	-	0/+

5.5. Option D: full redesign

Most of the building blocks of the scheme have been re-defined under option C. However, a number of respondents to the consultation suggested a broad expansion of the two other key building blocks of the scheme: the range of products covered and the preference margins. Thus, a full redesign is analysed: it includes the proposed changes under option C, and in addition changes to these two building blocks. In order to simplify the analysis, D sub-options are calculated as increments to C2 only. Three sub-options are assessed.

D1 is a far reaching option. It provides full product coverage expansion and elimination of all sensitive products (e.g., extending the duty-free, quota-free treatment of EBA countries) to all countries most in need (whether GSP or GSP+). This implies that the remaining beneficiaries are no longer subject to graduation.

D2 and D3 are less far-reaching. They take all the parameters of C2 (graduation included) and add partial desensitisation (D2) and partial expansion in product coverage (D3).

5.5.1. Option D1: full product coverage, full desensitisation

Effect on EU imports: trade creation and diversion

Option D1 implies a significant change—driven primarily by China (imports from which would increase by something like €16 billion), but also by other beneficiaries previously subject to significant graduation (e.g., India, Indonesia, Thailand, Vietnam). These exports would be spread amongst many sectors, the most salient of which are textiles, apparels, leather, rice, vegetables and fruit, and food products. With respect to B1, total imports would increase by about €14 billion, or by more than 1%. This implies that imports from other third countries – including other countries most in need, will have fallen. (see Annex 6.4 Table 6-4).

The aggregated impact on countries most in need would be positive. However, there would be large distributional effects, the additional space taken up by China, India, and other countries which were previously be subject to graduation would have a negative impact on many other countries most in need. EBAs in particular would suffer (a drop of around €750 million of their imports) (see Annex 6.4 Table 6-5), Bangladesh being the prime example—as would GSP+ countries such as Pakistan. In other words, the exports of the more competitive sectors (this is why they were graduated in the first place) take up the space of competing sectors in other countries which are less advanced. Countries less subject to competition from the imports which were previously graduated are less affected—or in some cases not at all.
In respect of other third countries, effects would also be negative on imports from many countries not subject to the scheme—almost across the board. However, imports would not appear to be significant as a percentage of EU imports in most cases.

These effects decrease under the hypothesis that all on-going negotiations have come into force (B2)—but contrary to most other options, the negative effects on the aforementioned countries would continue to be significant.

Effects on welfare, including EU consumer surplus
Assessment starts with the analysis of the effects as compared to baseline B1.

For countries most in need, welfare effects follow the sharply split pattern shown by exports within the category, with significant winners (China with +0.29%; Thailand with +0.84%), competitors which lose out (Bangladesh with -0.31%, Cambodia with -0.27%) and those competitors which are less affected by the emergence of the winners (Ecuador +2.39%, Ukraine +0.36%)[92]. Again, the undesired distributional effects crop up.

In respect of other third countries, by and large welfare impacts are not expected to be very significant, given that the share of imports affected is not high.

Unsurprisingly, the impact on EU welfare would not be noticeable. CARIS calculates a welfare loss of 0.05% even when all developing countries obtain full preferences— far beyond anything proposed under option D1. Changes in consumer welfare are not provided by CARIS, but an order of magnitude can be obtained from the SMART analysis. The consumer surplus increases by €12 billion, a significant amount or around 0.1% of the EU's GDP (see Annex 6.4 Table 6-4). This figure is larger than in other options and more significant.

If option D1 is compared with baseline B2, the impacts (both positive and negative) are lower, but would still be significant (both in the positive and negative sense) for beneficiaries—with the skewed distribution within the category as mentioned above.

Effects on production and employment: sectoral impacts
For this section, the analysis will concentrate on (1) the countries in the scheme where import and/or welfare impacts are significant[93]; and (2) on the EU. Wherever possible, the analysis will be based on CARIS.

As to beneficiaries (i.e., countries most in need), results are expected to be split, in line with export and/or welfare increases. CARIS[94] identifies a common denominator for all the countries which benefit: apparel and leather. While in the case of larger countries such as China and India these appear to be the key sectors affected, smaller exporters (e.g. Thailand) have significant increases in production and/or employment spread among many more sectors (e.g., rice, food). As for those who tend to lose out (e.g., Bangladesh), negative effects are more widely spread among sectors and are less significant individually. The apparel sector, however, is significantly affected by whatever measure. Ecuador and the Ukraine would benefit in the same sectors mentioned under option C.

The general picture underlined for option C would apply here as regards the EU—with the caveat that the effects would be spread more widely due to Chinese penetration of a significantly larger number of sectors.

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[92] See Annex 4 Table 4-9. The relevant column would be ZEROTM, which provides full preferences for all developing countries. This scenario will provide an accurate description for impacts on beneficiaries and on countries which were never subject to the scheme. For countries where preferences are deferred, this will not be accurate, so CARIS is not used.
[93] Impacts on production will be considered significant when they exceed 1%; on employment when they exceed 0.5%.
[94] ZEROTM scenario, as explained above.

While general effects are not expected to be significant, negative impacts on production and/or employment would occur in the rice, arable crops, oils and fats, sugar, fruit and vegetables, food products, apparel and textiles, and leather sectors. Once again, the main impacts would affect the later three sectors and the Member States mentioned under option C. Of the Member States, those with important agricultural production and food processing would be the most affected.

If option D1 is compared with baseline B2, the impacts (both positive and negative) are much lower given than the changes in imports are a third of those foreseen when comparing D1 with baseline B1. Once again, successful multilateral and bilateral negotiations will cause such profound impacts, that the scheme will have a limited residual influence.

Effects on EU tariff revenue
When compared to baseline B1, tariff revenue would decrease significantly—by about €12 billion (Annex 6.4, Table 6-4). The figure speaks for itself when compared to current tariff revenue (roughly €19 billion)[95]. The impact as compared to B2 would be smaller but still very significant—a drop of roughly €6 billion[96].

Effects on on-going trade negotiations
Providing such full access would undoubtedly create obstacles for negotiations, including EPAs.

Effects on the environment
Relative to baseline B1, imports rise under option D1. A negative direct effect on the environment (possible impact on greenhouse gas emissions, depletion of natural resources, and biodiversity losses) would result, although keeping in mind that trade would increase in the range of 1% only, it would still be moderate at worst.

Another possible negative effect is that, given that some GSP+ countries would lose exports, the support given by the scheme for sound environmental policies would be weakened.

This is the only option where imports in the longer run (B2) are increasing and significant. Thus, negative effects on the environment would extend also into B2.

Other effects
In respect of administrative costs[97], the effects are not expected to be significant. Increased trade would entail higher administrative costs, but the *de facto* disappearance of the three-tier system should decrease them. Less tariff revenue would also be collected—with a corresponding decrease in collection costs. On balance, no significant variations are expected.

This option includes improvements in the safeguard procedures, as well as in the procedures for GSP+ entry, monitoring and withdrawal procedures. This should improve the efficiency

[95] This does not take into account the impact of the trade agreements which have been initialled and are coming into force. If this were the case, the €19 billion figure would drop by around €1.5 billion.
[96] This does not take into account the impact of the conclusion of the multilateral round of negotiations, plus all the other on-going bilateral negotiations. If this were the case, the €19 billion figure would drop by around €14 billion.
[97] It is recalled that changes in preferential rules of origin are not analysed in this impact assessment.

and transparency of those mechanisms, providing for enhanced stability, legal certainty and predictability.

General assessment of economic, social and environmental effects

When compared to baseline B1, the general effects of option D1 are as follows.

Although the economic and social effects on countries most in need are expected to be positive as a whole – as under option C – these gains accrue mainly to those sectors which are already competitive, at the expense of those which are less advanced. The overall positive assessment ("+") must therefore be significantly nuanced.

The positive impact for EU consumers is likely to be compensated by lower tariff revenues, which are of the same order of magnitude. The net impact would thus be generated by impacts on producers. As explained above, these impacts would on the whole not be significant, but would have significant negative effects for important sectors—and for the EU Member States where they are important. As a result, these impacts would be negative overall. Although larger than under option C, they would probably be of a similar order of magnitude.

Environmental impacts in the EU would be marginally negative, given the overall increase in imports. The large increase in imports particularly in from China or India would lead to negative impacts in those countries also. The impact on GSP+ countries would be positive overall because, although their exports would increase, the environmental protection framework under which (all) businesses operate would be improved by adherence to the relevant environmental conventions. On balance, these effects would be marginally negative.

D1 vs. B1. Effects on:	**economic**	**social**	**environmental**
Countries most in need*	+	+	0/-
EU	-	-	0/-

*Positive economic and social impacts for countries most in need *as a whole* hide significant negative impacts on EBA and GSP+ beneficiaries.

When comparing the effects of option D1 to baseline B2, the changes would be expected to go in the same direction, only that they would become smaller—but still noticeable.

5.5.2. Options D2 and D3

These options build on option C. In order to simplify the analysis, only one of the options, in this case C2, has been used as a basis for D2 and D3. There is no reason to believe that noteworthy differences would exist if C1 were taken as a basis instead. Given that D2 and D3 change only one building block at a time with respect to C, only the salient novelties are mentioned here.

D2 and D3 generate preference erosion to the disadvantage of LDCs

D2 explores desensitisation. As expected, the immediate impact is preference erosion for EBAs, particularly vis-à-vis GSP competitors, which are the net winners. Given that the CARIS study made clear that there was a significant competitive pressure exerted by GSP countries on their EBA counterparts, this was to be expected. India, Indonesia, Vietnam and

Thailand absorb almost all the gains, while EBA countries capture almost none. As for GSP+ countries, the positive figure is counterintuitive, and is attributed to the limitations of partial equilibrium modelling described in Annex 6.3[98].

D3 explores product expansion. A similar impact as that described for D2 is recorded—benefits to GSP beneficiaries at the cost of preference erosion and export losses for EBA countries.

Both D2 and D3 thus confirm that product expansion and desensitisation have a price, a price which is paid by the poorest and which compounds the preference erosion they suffer.

D2 and D3 may place obstacles to negotiation of bilateral and multilateral agreements
Compared to option C, these options would arguably make our negotiating position more complex, by creating the expectation that concessions regarding the products which have come into the scheme or have been desensitised can be obtained from the EU automatically.

The size of the changes introduced by D2 and D3 are not sufficiently large as to vary the order of magnitude of the rest of the results of option C. However, EU producers of additional products under the scheme and of those goods which receive higher preference margins via desensitisation, will suffer additional pressure.

6. COMPARING THE OPTIONS

6.1. Review of different options by objectives and impacts

The following table compares how well the different options examined above meet the objectives sought by a review of the scheme. This comparison is based on three criteria: effectiveness (number of objectives met, to what degree); efficiency (use of resources necessary to meet the objectives, unintended spill-over effects); and consistency with overarching EU objectives.

Criterion	**Policy Options**					
	A	**C1**	**C2**	**D1**	**D2**	**D3**
General Objective G1: *Contribute to poverty eradication by expanding exports of countries most in need*	--	++++	++	--	+	+
General Objective G2: *Promote sustainable development and good governance*	---	+++	++++	---	+++	+++
General Objective G3: *Ensure better safeguard for EU's financial and economic interests*	++++	+++	+++	---	++	++
(Overall) Effectiveness	-	++++	+++	--	++	++
Efficiency	--	+++	++	--	+	+
Consistency	++++	++	++	---	+	+

[98] In fact, they have to do with imports from Ecuador, where the aggregation of TARIC 8 digit codes into the HS 6 digit codes used by the SMART model produce a distortion with respect to the desensitised codes.

A detailed analysis follows, based on the sub-objectives and salient problems.

6.2. Option A

Objective G-1: Contribute to poverty eradication by expanding exports of countries most in need

At best, this option meets this objective only in part, and inefficiently.

While option A focuses preferences on some of the countries most in need (LDCs), it leaves also many other countries with similar trade, development and financial needs without preferences. Thus, a refocusing of preferences (specific objective S-1) is only achieved in part and at the cost of preference loss (and negative economic and social impacts) for many countries in need. This is also contrary to the overarching policy objective of contributing to development according to the needs of our partners (see 2011 CWP, p. 9).

In addition, removing preferences from some of the countries most in need will leave many export sectors more open to competition from more developed countries. Given the large competitive pressure which the latter exert on countries most in need, a number of export sectors in needy countries are bound to suffer significantly—or even to disappear. Thus, this option creates disincentives to diversification—the contrary of specific objective S-2.

Objective G-2: Promote sustainable development and good governance

The elimination of GSP+ removes the scheme's support to sustainable development and good governance—the contrary of specific objective S-4.

Objective G-3: Ensure better safeguard for EU's financial and economic interests

Option A does nothing to improve the efficiency of the safeguard instrument (S-5). Even though many potential competitors of EU industry would be removed from the system, LDCs are significant exporters in certain sectors (e.g., textiles), which would necessitate efficient, predictable safeguard mechanisms.

On the other hand, an unintended by-product of this option would be a stronger negotiating position in the multilateral and bilateral context (S-3). This would be in line with the 2011 Commission’s Work Programme objectives (see its p. 8), which were also an integral part of the Future of Trade Policy Communication. Also, economic and social impacts are positive due to the improvement in certain industrial sectors and Member States. This fits in with the Commission’s emphasis on boosting competitiveness, growth and job-creation—as well as dealing with the economic crisis and building the momentum of the recovery (see 2011 CWP, p. 3). In a period of austerity and increasing pressure on the budget, another positive effect is that tariff revenue increases.

On the whole, the impact is rather positive—and generally consistent with a number of broader policy objectives and priorities.

6.3. Option C

6.3.1. Option C1

Objective G-1: Contribute to poverty eradication by expanding exports of countries most in need

Option C1 benefits from the common pillars of option C. It effectively targets those most in need, in two ways. First, preferences respond positively to concrete needs—with the result that preferences are deferred for sufficiently rich beneficiaries, and for those which enjoy similar access via bilateral agreements. Second, more advanced sectors which do not require preferences to penetrate the EU market are weeded out more efficiently *via* higher graduation. This ensures that preferences are properly focused (S-1): only those countries and sectors most in need benefit. Given that the competitive pressure of less needy beneficiaries hindered the use of preferences by those most in need, this option would also open the door to a more intensive use of preferences by the latter. Also, the same pressure placed obstacles to diversification—obstacles which would thus be removed (S-2). The level of preference utilisation would also increase.

The foregoing would happen efficiently, in the sense that countries or sectors which deserve preferences by and large remain as beneficiaries. On top of the foregoing, another factor would contribute to efficiency: the redefinition of product sections would avoid the situation where less competitive products within the category are graduated as 'collateral damage'.

Nonetheless, as regards efficiency, it is important to underline two differences between options C1 and C2.

First, graduation is significantly higher for some countries under option C2, given that the graduation thresholds are significantly lower. If a similar overall result is achieved by a higher graduation threshold, it would be more efficient to opt for the latter.

Second, the more GSP+ beneficiaries enter into the system, the more competitive pressure will exist on LDCs—the neediest of all developing countries. In this context, C1 results in less pressure on LDCs than C2. It may be more efficient to retain C1 for this purpose.

This option is thus in line with the overarching policy objective of contributing to development according to the needs of our partners (see 2011 CWP, p. 9).

Objective G-2: Promote sustainable development and good governance

Option C1 again benefits from the common pillars of C. The combination of a more flexible entry mechanism as regards conventions, more flexible trade criteria for eligibility, and no graduation for GSP+ beneficiaries, would boost the power of the scheme to promote sustainable development and good governance, in line with specific objective S-4. While effectiveness would be high, it should be underlined that this option does not include a review of the conventions list, which would further enhance effectiveness.

Efficiency should be nuanced. As explained above, broader GSP+ membership would have a negative impact on LDC exports.

Objective G-3: Ensure better safeguard for EU's financial and economic interests

Option C1 improves the efficiency of the safeguard instrument (S-5) and of the withdrawal mechanisms for beneficiaries. Both would enhance legal certainty and predictability of the scheme (S-6), and safeguard the EU’s financial and economic interests.

As under option A, an unintended by-product of this option would be a stronger negotiating position in the multilateral and bilateral context (S-3)—albeit with respect to a lower number of countries than emerges under option A. This would also be in line with the 2011 CWP objectives (see its p. 8), which were moreover an integral part of the Future of Trade Policy Communication.

On the positive side again, tariff revenue increases in a period of budgetary pressure.

The foregoing should be balanced, however, with the negative economic and social impacts on certain sectors and Member States. This would not help competitiveness, growth and job-creation, particularly in a period where so much effort is being put towards economic recovery.

On the whole, the balance of impacts would be positive. Consistency with broader policy objectives and priorities would be mixed, although also positive.

6.3.2. Option C2

Given that most building blocks are common to options C1 and C2, only noteworthy differences are highlighted here.
Regarding the efficiency of objective G-1 (contribute to poverty eradication by expanding exports of countries most in need), there are two salient differences.

To start with, the much lower graduation thresholds in C2 reduce total exports by countries most in need in our static analysis, as explained above. While dynamic effects should compensate for this fall, it is an indication that the 7.5% graduation threshold may be excessive to achieve the intended objective.

In addition, the more GSP+ beneficiaries enter into the system, the more competitive pressure will be exerted on LDCs—the neediest of all developing countries. In this context, C1 provides less pressure on LDCs than C2. It may be more efficient to retain C1 for this purpose.

Regarding the effectiveness of objective G-2 (promote sustainable development and good governance), this option is superior to C1 as it includes a revision of conventions.

The foregoing indicates that C2 as a whole would be inferior to C1, but still retain positive aspects.

6.4. Option D: full redesign

6.4.1. Option D1

Objective G-1: Contribute to poverty eradication by expanding exports of countries most in need

This option targets those most in need by deferring preferences for sufficiently rich beneficiaries, and for those which enjoy similar access via bilateral agreements.

However, it achieves the opposite in many other ways. To start with it eliminates graduation for all beneficiaries—with the implication that more advanced sectors which do not require preferences to penetrate EU market will nonetheless receive them. This leads to increasing pressure precisely on those competing sectors which are less advanced and do need preferences. In addition, the extension of EBA treatment to all beneficiaries accelerates preference erosion for the poorest beneficiaries. Therefore, option D1 does not lead to a proper focusing of preferences (S-1).

Also, the aforementioned pressure creates further obstacles to diversification, as advanced sectors put pressure on competing producers in other countries most in need. Thus, S-2 is not met. Finally, as explained above, competitive pressure by the more advanced also impinges upon utilisation of preferences by those most in need.

In consequence, this objective is not met overall.

This option would also not be in line with the overarching policy objective of contributing to development according to the needs of our partners (see 2011 CWP, p. 9).

Objective G-2: Promote sustainable development and good governance
GSP+ is an incentive-based mechanism. Yet, option D removes this incentive by granting it unconditionally to every beneficiary regardless of any other formal improvements of the scheme (e.g., more flexible entry). This is contrary to the objective of promotion of sustainable development and good governance.

Objective G-3: Ensure better safeguard for EU's financial and economic interests
As under option C, option D1 improves the efficiency of the safeguard instrument (S-5) and of the withdrawal mechanisms for beneficiaries. Both would enhance legal certainty and predictability of the scheme (S-6), and safeguard the EU’s financial and economic interests.

On the negative side, tariff revenue decreases significantly in a period of budgetary pressure. This adds to the negative economic and social impacts on certain industrial sectors and Member States. This would not help competitiveness, growth and job-creation, particularly in a period where so much effort is being put towards economic recovery.

In addition, this option would have severe unintended effects, by weakening the EU's negotiating position in the multilateral and bilateral context (S-3). This would not be in line with the 2011 CWP objectives (see its p. 8), which were also an integral part of the Future of Trade Policy Communication.

On the whole, the balance of impacts would be rather negative. Consistency with broader policy objectives and priorities would also not be ensured.

6.4.2. Options D2 and D3

These two options share the same basic traits as those described under option C. Only the aspects that differ from C are described here.

D2 and D3 are less efficient than C, as they increase imports of GSP beneficiaries at the cost of EBA countries, precisely the set of countries with the largest trade, development and financial needs.

In addition, they render the EU's position more complex in bilateral and multilateral negotiations by giving a signal that the tariffs on new or desensitised products are not important for the EU.

This implies that options D2 and D3 will be inferior to C.

6.5. Preferred option

The option which meets the objectives of the scheme in the most effective, efficient and consistent manner is C, and in particular C1. This does not negate that C2 contains positive aspects (review of the list of conventions) which can also be considered.

7. MONITORING AND EVALUATION

The table below includes suggestions for indicators that can be used to assess the progress and effectiveness of the preferred option in achieving general policy objectives.

General Objectives	Indicators	Sources of information
To contribute to poverty eradication by expanding exports from countries most in need	- expansion of developing countries exports to EU - increased share of imports from countries most in need - increased utilization of the preferences - effective graduation of the competitive sectors -increasing diversification	- Eurostat data
To promote sustainable development and good governance	- increased number of countries committing to sustainable development and good governance principles within GSP+ arrangement - overall improvement of implementation of GSP+ conventions by GSP+ beneficiaries -number of withdrawals	- reports of relevant international monitoring bodies -DG TRADE
To ensure a better safeguard for the EU's financial and economic interests.	-number of safeguard requests -number of safeguard measures -revenue foregone due to the scheme -number of preferential trade agreements signed with beneficiaries - number of preferential trade agreements signed with non-beneficiaries	-Safeguard requests -Eurostat data -DG TRADE

The effectiveness of the GSP scheme introduced by the proposed new regulation should be subject to formal and independent evaluation prior to any subsequent revision. To be effective, such evaluation is likely to require a minimum of 3 years' post-implementation data, which implies that the evaluation cannot take place before the end of 2017 at the earliest.

ANNEXES SEE SEPARATE DOCUMENT