

**INTERNATIONAL TRADE DISPUTE SETTLEMENT
IN GATT/ WTO
WITH SPECIAL REFERENCE TO JAPAN.**

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***To my beloved parents,
Yuji Takahashi and Shizuko Takahashi,
for their consistent support, encouragement
and strong belief in my challenge***

and

***in the affectionate memory of
Kikuko Takahashi.***

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Finally, it goes without saying that the views expressed in this dissertation are entirely personal and the remaining errors and inaccuracies are my own.

ABBREVIATIONS

Am. Soc'y Int'l L. Proc.	American Society of International Law Proceedings
Am. J. Int'l L.	American Journal of International Law
Arb. J.	The Arbitration Journal
BISD	Basic Instrument and Selected Documents of the GATT
BNA, ITR	Bureau of National Affairs, International Trade Reporter (Washington)
Brit. Y. B. Int'l L.	The British Year Book of International Law
Brook J. Int'l L.	Brooklyn Journal of International Law
Cal. W. Int'l L.J.	California Western International Law Journal
Case W. Res. L. Rev.	Case Western Reserve Law Review
Colum. J. Transnat'l L.	Columbia Journal of Transnational Law
C.M.L.Rev.	Common Market Law Review
Cornell Int'l L. J.	Cornell International Law Journal
Dick. J. Int'l L.	Dickson Journal of International Law
Disp. Resol. J.	Dispute Resolution Journal
DSB	Dispute Settlement Body
DSU	Dispute Settlement Understanding (Annex 2 of the WTO Agreement)
EC	European Community
ECJ	European Court of Justice
EJIL	European Journal of International Law
EU	European Union
Emory Int'l L. Rev.	Emory International Law Review
Eur. Env'tl. L. Rev.	European Environmental Law Review
Fordham Int'l L. J.	Fordham International Law Journal
Fordham L. Rev.	Fordham Law Review
Ga. J. Int'l & Comp. L.	Georgia Journal of International and Comparative Law
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
GATT 1947	GATT concluded in 1947
GATT 1994	GATT incorporated into the 1994 Agreement on the WTO
Geo.Wash. J.Int'l L.& Econ.	The George Washington Journal of International law and Economics

Germ. Y. B. Int'l L.	German Year Book of International Law
Harv. Int'l L. J.	Harvard International Law Journal
ILSA J. Int'l & Comp. L.	ILSA International and Comparative Law
Int'l Affairs	International Affairs
Int'l Comp'y & Com'l L.Rev.	International Company and Commercial Law Review
Int'l Law.	The International Lawyer
I.L.M.	International Law Material
IMF	International Monetary Fund
Int'l Org.	International Organisation
Int'l Quart.	International Quarterly
Int'l & Comp. L.Q.	The International & Comparative Law Quarterly
Int'l Tax & Bus. Law.	International Tax & Business Lawyer
Japan. Ann. Int'l L.	The Japanese Annual of International Law
J. Int'l L. & Practice	Journal of International Law and Practice
JCMS	Journal of Common Market Studies
JIEL	Journal of International Economic Law
J.W.T.L. (J.W.T. since '88)	Journal of World Trade Law
Law & Pol'y Int'l Bus.	Law and Policy in International Business
LJIL	Leiden Journal of International Law
MAFF	Ministry of Agriculture, Forestry and Fisheries (of the Government of Japan, "GOJ")
Md. J. Int'l L.	Maryland Journal of International Law
Md. J. Int'l L. & Trade	Maryland Journal of International Law and Trade
MFN	Most-Favoured-Nation
Mich. L. Rev.	Michigan Law Review
Mich. J. Int'l L.	Michigan Journal of International Law
Minn. J. Global Trade	Minnesota Journal of Global Trade
Minn. L. Rev.	Minnesota Law Review
MITI	Ministry of International Trade and Industry (of the GOJ)
Mo. L. Rev.	Missouri Law Review
MOF	Ministry of Finance (of the GOJ)
MOFA	Ministry of Foreign Affairs (of the GOJ)
MTN	Multilateral Trade Negotiations
NBL	New Business Law (in Japanese)

N.C. J. Int'l L. & Com. Reg.	The North Carolina Journal of International Law and Commercial Regulation
Neths. Y. B. Int'l L.	Netherlands Year Book of International Law
NTB	Non-Tariff Barrier
N.Y. Int'l L. Rev.	New York International Law Review
Nw. J. Int'l L. & Bus.	Northwestern Journal of International Law and Business
Nw. J. Int'l T.	Northwestern Journal of International Trade
OECD	Organisation for Economic Cooperation and Development
OJ	Official Journal of the European Communities
RECIEL	Review of European Community and International Environmental Law
SPS	Sanitary and Phytosanitary Measures
Stan. J. Int'l L.	Stanford Journal of International Law
Sw. Rev. Int'l Comp'n L.	Swiss Review of International Comp'n Law
Tex. Int'l L. J.	Texas International Law Journal
Tm. W.	The Trademark World
TRIPS	Trade Related Intellectual Property Rights
TPRB	Trade Policy Review Body
TPRM	Trade Policy Review Mechanism
TRIMS	Trade Related Investment Measures
UCLA L. Rev.	UCLA Law Review
USTR	United States Trade Representatives
Vand. J. Transnat'l L.	Vanderbilt Journal of Transnational Law
Va. J. Int'l L.	Virginia Journal of International Law
VER	Voluntary Export Restraint
VRA	Voluntary Restraint Arrangement
W. Compet'n.	The World Competition
W. Econ.	The World Economy
WTO	World Trade Organisation
Yale L. J.	Yale Law Journal

ABSTRACT

The principal aim of this thesis is two-fold: first, to examine the way the GATT/WTO dispute settlement system has evolved, and secondly, to highlight those disputes in which Japan was involved. This later is done to demonstrate the clear transformation of Japan's attitude vis-à-vis its trade disputes falling within the GATT or WTO dispute settlement framework.

Although the GATT dispute settlement mechanism has been fairly successful, the recent refinements have taken almost half century to accomplish: the GATT was gradually strengthened and finally superseded by the WTO which provides for a "judicialised" dispute settlement mechanism. This development has been hailed as providing for a much more "secure", "predictable" and "effective" system for settling trade disputes.

Articles XXII and XXIII of the GATT and the Understanding on Rules and Procedures Governing the Settlement of Disputes constitute the core of the first part of the thesis. The case study, which is undertaken in part two of the thesis, is limited to those disputes in which Japan was a litigant party.

Part one consists of 5 chapters: Chapters 1, 2 and 3 examine the old GATT and its dispute settlement system, including the Uruguay Round negotiations on dispute settlement. Chapters 4 and 5 discuss the WTO and its dispute settlement mechanism as clarified and codified in the Understanding.

Part two consists of 3 chapters: Chapter 6 provides a brief description of the Japanese legal system; Chapter 7 and 8 discuss the cases in which Japan was a party. Although the aim of the case study is to provide a legal analysis of those cases, it also attempts to demonstrate the shift in Japanese trade policy regarding its disputes in the context of GATT on the one hand and the WTO on the other. The proposition put forward here is that such a shift has been from a "power-oriented" or "bilateral" to a more "rule-oriented" or "multilateral" one; thus reflecting the changes taken at the institutional level.

**I, Tsutomu Takahashi,
certify this dissertation
to have been composed
by myself and to be my own work.**

INTRODUCTION

"Disputes are an inevitable part of international relations, just as disputes between individuals are inevitable in domestic relations. Like individuals, states often want the same thing in a situation where there is not enough of it to go around.

...

Disputes, whether between states, neighbours, or brothers and sisters, must therefore be accepted as a regular part of human relations and the problem is what to do about them".¹

This dissertation examines the dispute settlement ("DS") system of the "old" GATT and the "new" WTO.² Its main aim is to show how this DS system has evolved from political to legal nature. It further examines the main disputes in which Japan was involved under both GATT and WTO.

In conducting the above examination, I have consulted a large number of primary and secondary materials, including GATT/WTO official documents, in the form of decisions, agreements or understandings; panel and appellate body reports; the agreements of negotiation rounds; ministerial decisions and declarations; working papers on DS of the Uruguay Round ("UR");³ interviews; practical experience;⁴

¹Merrills, J. G., International Dispute Settlement, 2nd ed., Grotius Publications Limited, Cambridge, 1991 at 1.

²For a brief chronology of some of significant events and achievements in the multilateral trading system (GATT/WTO), see "Golden Jubilee of the Multilateral Trading System" in **PRESS/88** (5 February 1988).

³To obtain official (then restricted) documents of GATT, I carried out a series of research trips to the GATT/WTO Secretariat in Geneva during my research period: the first time in April 1994; the second time in October 1994; the third time in September 1996; the fourth time from April through June 1997 (during the period of my internship); and the most recent visit in June 1998; The Uruguay Round (1986-94), initiated on 22 September 1986 in Punta del Este, Uruguay, has been characterised as "[t]he most complex and ambitious programme of negotiations ever undertaken by GATT", see GATT, News of the Uruguay Round of Multilateral Negotiations, October 1986 at 1. The countries participated in this round have been increasing gradually: 103 (countries) in 1986, 117 by end of 1993 and finally reached until 128 by early 1995. Negotiations at the Uruguay Round was far more ambitious in comparison with previous rounds because of a number of reasons, especially: (i) the opening of new areas for negotiation, such as agriculture, fibre, and services; (ii) the potentially higher impact on national policy of the negotiations; for the previous rounds of negotiations are: 1st Round (1947) at Geneva; 2nd Round (1949) at Annecy; 3rd Round 1950-51) at Torquay; 4th Round (1955-56) at Geneva; 5th Round named "The Dillon Round" (1960-61) at Geneva; 6th Round called "The Kennedy Round" (1964-67) at Geneva; 7th Round entitled "The Tokyo Round" (1973-79).

⁴Practical experience was obtained through my internship at the Legal Affairs Division of the WTO Secretariat from April to June 1997.

monographs; articles in periodicals, magazines, or newspapers; the Internet and so forth.

The old GATT DS system was criticised for its "ambiguity", "complexity" and "ineffectuality". The reasons for these criticisms were various: for instance, its *de facto* origin; the limited scope of the system, i.e., dealing only with trade in goods; and the strong "political" or "power-oriented" (instead of "judicial" or "rule-oriented")⁵ nature of the DS mechanism as a whole.⁶

Moreover, the GATT DS system consisted of a number of DS procedures found in various parts of the General Agreement and related legal instruments, though the principal and formal DS procedures were found in Articles XXII and XXIII of GATT. Article XXIII, in particular, a pivotal provision of the DS system even under the WTO, contained little information apart from three forms of causes of action. The procedures for implementing the DS rules of GATT have, therefore, evolved gradually during nearly half a century of GATT practice, and have developed into an elaborate, not to say labyrinthine, DS system.

This work looks at whether the above criticisms have been dealt with and it also traces the evolutionary process of the GATT/WTO DS regime.

Two main themes emerge in this work: (i) how the GATT/WTO DS system has evolved during nearly five decades and (ii) how Japan has shifted its policy on DS during the evolution at the institutional level.

⁵For the discussion of "power-oriented" and "rule-oriented" diplomacy, see Jackson, John H., Restructuring GATT System, Pinter Publisher, London, 1990, pp. 49-54, 56ff; Jackson J.H., The World Trading System: Law and Policy of International Economic Relations, The MIT Press, Cambridge, Massachusetts, 1989; and for the distinction between dispute settlement systems with a "adjudication" nature (focusing on an enforcement of rules) and "negotiation" nature (aiming at settlement), see generally, Davey, William J., "Dispute Settlement in GATT", 11 *Fordham Int'l L. J.* Number 1, fall 1987, pp. 51-109.

⁶This is why the less-developed contracting parties found the system unfair, unpredictable and unreliable, and accordingly, the GATT DS system was unpopular among those members.

With respect to the first theme, a series of agreements signed at multilateral trade negotiations demonstrates the development of *de facto* GATT rules into more elaborate and complex DS rules.⁷ For instance, the UR set a significant landmark by consolidating the decisions, procedures and customary practices for a period of almost a half of a century.

The second theme is examined through a case study. The case study part starts with a basic overview of the legal structure of Japan, which will enable us to understand the legal status of GATT/WTO within the Japanese legal context. The study highlights the impact which GATT/WTO had on the domestic cases of Japan. The GATT/WTO cases examined in Chapters 7 and 8 were carefully selected and ordered chronologically to demonstrate the shift from a "power-oriented" or "bilateral" to a "rule-oriented" or "multilateral"⁸ approach in Japan's policy towards DS under GATT/WTO.

With regard to the structure of the dissertation, the dissertation is divided into two parts. The first part consists of the first five chapters which deal with GATT and WTO and their DS systems. The second part, which consists of the last three chapters, examines Japan's developing experience of GATT/WTO DS based on case studies.

⁷See, Chapter 2, Sections 2.4. and 2.5. of this thesis.

⁸*Multilateralism* is an approach to the conduct of international trade based on co-operation, equal rights and obligations, non-discrimination and the participation as equals of many countries regardless of their size or share of international trade, while *Bilateralism* is a preference for conducting international trade policy making through direct bilateral negotiations. The latter approach works more in favour of the strong (economically and politically) and against the interests of small/medium-sized countries. (these definitions are from Walter Goode, Dictionary of Trade Policy Terms, Second ed., The Centre for International Economic Studies, University of Adelaide, Australia, 1998 at 34, 187).

Multilateralism is the foundation of rules and principles embodied in the Marrakesh Agreement Establishing the World Trade Organisation and its components (i.e. "the WTO Agreement"). In reality, however, bilateralism would be an easier and/or more effective approach to obtain results because, in principle, it involves fewer diverting factors. Nevertheless, this approach could introduce further conflicts or tensions with other parties under the Multilateral System. Moreover, bilateralism could even undermine or damage the whole WTO system including its DS system. In this thesis, "bilateralism" and "power-oriented" are used synonymously, likewise "multilateralism" and "rule-oriented" in describing member states' approaches towards their DS. See, an explanation for the terms, i.e. "rule-oriented" and "power-oriented" diplomacy in, *supra* note 5.

The study begins with an examination of the old GATT, which provides not only overview of the GATT system but also identifies problems inherited from its unfortunate start. Then the focus will be on the old DS system. This part seeks to identify the main "defects" of the system and further endeavours to demonstrate the evolutionary process of the DS system towards "judicialisation" based on the official GATT documents on DS. Likewise, the investigation will continue with regards to the new WTO system and its DS system to highlight the evolution in the two different systems. Finally, the research leads to a case study in the second part of the dissertation. The choice of Japan in this case study is not simply because of my personal background (as a Japanese) but, more importantly, Japan's emerging use of DS mechanisms under the GATT/WTO. This study is confined to examining Japanese cases, and particularly, significant ones which are essential to demonstrate Japan's transformation in its trade policy on DS. Furthermore, due to its importance in highlighting a shift in the Japanese policy on DS, the study also includes a few disputes which were eventually settled bilaterally or which were withdrawn for a political reason. The cut-off date of the WTO case study applied in this thesis is 30 June 1998, however, those new cases whose reports have been issued after this date are attached to the thesis as Appendix III. This Appendix does not intend to discuss or examine those cases but simply to provide a summary respectively. In addition, to grasp the Japanese history of DS under the GATT/WTO system, the Appendix IV lists other disputes (i.e. some are active or pending, the others are settled bilaterally or withdrawn) in which Japan has been involved (except those cases in which Japan has participated as a third party).

PART ONE
INTERNATIONAL TRADE DISPUTE SETTLEMENT
MECHANISM

Chapter 1. AN INTRODUCTION TO THE OLD GATT LEGAL
SYSTEM

Introduction

This chapter offers a general introduction to the institutional structure as well as main principles of the old GATT. The GATT system is an evolutionary one, this system and a number of features have survived after it has been superseded by the new system of WTO. It is therefore essential for us to understand the structures of GATT to begin with in order to understand the new WTO system which will be investigated later in the Part One.

1.1. Institutional Structure¹

The General Agreement on Tariffs and Trade (hereinafter, the "1947 GATT"), concluded in October 1947, was a multilateral trade agreement which provided for a substantial reduction of tariffs among contracting parties, together with a code of general rules to control a variety of other trade restrictions (e.g. non-tariff barriers including balance-of-payments restrictions). The fundamental intention of the GATT was to provide "freer and fairer international trade" through the reduction of tariffs and elimination of other trade barriers. In addition, the structure of GATT as an organisation developed gradually because of its difficult start.

¹For the complete list of GATT bodies, see, the Secretariat, GATT Directory; Long, Olivier., Law and its limitations in the GATT Multilateral Trade System [hereinafter, the "Law and Limitations"], Martinus Nijhoff Publishers, Dordrecht, the Netherlands, 1987.

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1.1.1. The Contracting Parties

The Charter of the International Trade Organisation ("ITO Charter" or "Havana Charter"), which never entered into force because the United States Congress failed to approve it, made provisions, for both the institutional and administrative structure of GATT. The GATT was originally designed as a principal multilateral treaty of international trade not as an organisation. The GATT, however, was set up with its own institutions and *de facto* administrative staff.² The Contracting Parties³ were the only institutional body recognised when the General Agreement first became effective on 1 January 1948 in accordance with the terms of the Protocol of Provisional Application.⁴

The Contracting Parties⁵ had power to legislate under GATT: for example, they adopted Part IV (Trade and Development) of the General Agreement and they modified certain articles, for example, GATT Article XVIII (Government Assistance to Economic Development). The GATT conferred several powers upon the Contracting Parties, such as the authority to hold consultations with respect to any matter; the authority to put questions to the disputing parties as regards information, reports, and consultations; the authority to investigate matters referred to them; the authority to consult with the disputing parties, to make recommendations, and to authorise the suspension of obligations and concessions; to waiver authority; to authorise negotiations and renegotiations; the authority to specify that an amendment

² See for a history of the Secretariat, Section 1.1.6. (The Secretariat) of this chapter.

³ The term "Contracting Parties" was widely used in GATT communiqué and in literature on the GATT.

⁴ On 30 October 1947, twenty-three countries signed a Final Act authenticating the text of the General Agreement on Tariffs and Trade (55 UNTS 194). At the same time when countries signed the GATT, the eight main participants in the negotiations concluded a Protocol of Provisional Applications (PPA) in Geneva, 30 October 1947, and came into force as on 1 January 1948: 55 UNTS 308; reproduced in **BISD IV/77**.

⁵ In this thesis, when the expression "Contracting Parties" is used in the upper case (CONTRACTING PARTIES) [hereinafter, the "CP" or "CPs"] it means that they are considered to be acting jointly and in a formal manner in terms of the relevant articles of GATT. On the other hand, the terms "Contracting Parties" in lower case (contracting parties) means that a collection of individual countries who are the signatory to the General Agreement are being referred to; cf. As defined in GATT Article XXV:1, "Whenever reference is made in this Agreement to the contracting parties acting jointly they are designated as the CONTRACTING PARTIES".

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was important enough to let non-signatories free to withdraw, or to enable non-signatories to remain a contracting party with the consent of the CONTRACTING PARTIES; and to authorise anti-dumping and countervailing measures.

The powers conferred by GATT on its signatories were as follows: the authority to co-operate with and to perform certain functions of the International Monetary Fund (hereinafter, the "IMF"); the authority to review quantitative restrictions; the authority to request information regarding (as well as review of) domestic administrative review relating to customs matters; the authority to look into non-tariff barriers, import restrictions for reasons of balance of payments and regional integration; and the authority to enter into agreements for the accession of new parties to the system.⁶

The Contracting Parties met from time to time for the purpose of giving effect to those provisions of the GATT which involved joint action and, more generally, with a view to facilitating the operation and furthering of the objectives of the Agreement.⁷ Such meetings were named "Sessions" and were usually held annually. Sessions of the Contracting Parties were not open to the public, though, the public was kept informed by means of communiqués and sometimes by inviting the media to press conferences. Decisions were taken by a simple majority, except when it was otherwise provided for in the GATT.⁸

1.1.2. The Council of Representatives

The Council of Representatives (hereinafter, the "Council") was established by a decision of the CPs on 4 June 1960.⁹ Legally, it acted as the Contracting Parties' intersessional body which replaced the Intersessional Committee. It was authorised

⁶See Jackson, John. H., World Trade and the Law of GATT [hereinafter, the "Law of GATT"], The Bobbs-Merril Company, Inc., Indianapolis, 1969, pp. 128-132.

⁷GATT Article XXV:1.

⁸For example, GATT Articles XXIV:10, XXV:5, XXX, and XXXIII.

⁹BISD 9S/8.

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to take up all the questions with which the Contract Parties dealt at their sessions including urgent matters, and it was also authorised to set up any necessary subsidiary bodies as well as to prepare the sessions of the Contracting Parties. The Council supervised the work of the committees, working parties, and other subsidiary GATT bodies. In addition, it also examined reports of those subsidiary bodies and made appropriate recommendations. Any representative of a contracting party could be a member of the Council upon their request. The Chairman of the Council was elected by the Contracting Parties for the period of one year.

In terms of the procedures of dispute settlement, the Council or its Chairman was in charge of appointing the panel members. The Council determined the terms and reference of the panel and adopted their reports. This meant that in some instances the Council had a quasi-judicial responsibilities. Nonetheless, it was only when the Contracting Parties adopted the annual report of the Council that any panel interpretation of the GATT provisions referred to in that report became legally authoritative.

The Council in its part was the intersessional body and the executive organ of the Contracting Parties. It performed its role in the activities of GATT from 25 November 1968.¹⁰ The Council became the central body directing the activities of GATT, holding an average of nine meetings a year. A meeting could be summoned at short notice without any delay or difficulty, since the member countries had permanent representatives in Geneva. This facilitated frequent communication between the Council members and the Secretariat in preparing the work of the Council.

¹⁰Twenty-fifth session of the Contracting Parties, 25 November 1968, SR 25/9 (December 1968) at 176.

1.1.3. Other Important Bodies of GATT - "Permanent/Non-Permanent"

There were also other essential bodies within the GATT, whether permanent¹¹ or non-permanent, such as Committees, Working Parties, and Panels. This section will examine them in turn.

1.1.3.1. Committees

The Committees were established to examine important questions in depth and usually on a continuing basis. In general, committee membership was open to all contracting parties. Some of those committees were standing committees such as the Committee on Balance of Payments Restrictions, the Committee on Tariff Concessions, the Committee on Safeguards, and the Budget Committee. Membership to those committees was, however, limited and determined by the Council. In addition to those Committees, there was the Committee on Trade and Development, whose Chairman was elected by the Contracting Parties, and traditionally appointed from a developing country. Chairmen of other committees, on the other hand, were appointed by the Council. Furthermore, some committees were not permanent, such as the Committee on Trade Negotiations. All committees supervised the conduct of the multilateral negotiations undertaken by the Contracting Parties. The Director-General (hereinafter, the "DG") of GATT chaired these committees with the aim of ensuring their independence and impartiality according to the wording of GATT. Finally, there were other types of committees and councils which had not been established either by the Contracting Parties or by the Council but established under the Tokyo Round agreements and the Multifiber Arrangement (hereinafter, the "MFA").

¹¹ Permanent bodies were, for example, Consultative Group of Eighteen, Committee of Balance of Payments Restrictions, Committee on Tariffs Concessions, Committee on Safeguards, Committee on Budget Finance and Administration, and Joint Advisory Group on the International Trade Centre (UNCTAD/GATT).

1.1.3.2. Working Parties

The Working Parties were temporary bodies which dealt with some important questions including disputes which arose between contracting parties. The Council established the Working Parties and provided them with the terms of reference for their tasks. The Working Parties submitted reports and conclusions as advisory opinions to the Council, which were normally adopted in the form they were made available to the Council. It could be considered that as their conclusions were the result of consensus achieved through negotiation or compromise, the Council was, accordingly, in a position to adopt the recommendations of the Working Parties. Any interested member country including those who were in dispute could become a member of the Working Parties. At the Second Session in 1948 (Geneva), the first Working Party was set up to comment upon a dispute between the U.S. and Cuba concerning Cuba's textile regulations.¹²

1.1.3.3. Panels

The origin of the panel procedures goes back to the Seventh Session (1952) where it was adopted.¹³ However, the practice of panel members' appointment in an individual capacity commenced only at the Ninth Session (1955).¹⁴ The main function of the panel was to prepare an independent assessment of the facts of the case. A panel would normally try to promote conciliation between the parties to the dispute with the goal of achieving the withdrawal of the action or measure subject to complaint. The panel, unlike the members of Committees and Working Parties (whose membership was open to any member who had an interest), was in principle composed of persons in their individual capacities who did not represent their governments.¹⁵ Panel members were usually appointed from the members of national

¹² See, GATT/CP.2/SR.22(complaint); GATT/CP.2/SR.23(a request for a working party); GATT/CP.2/43(settlement).

¹³ Seventh Session (2 Oct.-10 Nov. 1952), SR.7/1-17.

¹⁴ Ninth Session (28 Oct. 1954 - 8 Mar. 1955), SR.9/1-47.

¹⁵ Cf. The panel consisted of three to five members (panellist) who should preferably be governmental as stipulated in *Understanding Regarding, Notification, Consultation,*

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delegations to the GATT, but not from among the nationals of a country whose government was one of the disputing parties.¹⁶ In this respect, the panel system marked the beginning of the process of transformation of the GATT from a forum of (political) negotiation to one providing impartial adjudication.

1.1.4. The Consultative Group of Eighteen

On 11 July 1975, the Council decided to establish the Consultative Group of Eighteen (hereinafter, the "Group") on a temporary basis,¹⁷ which later became permanent in 1979.¹⁸ The membership of the Group was restricted to eighteen member countries. The DG of GATT chaired the group if this was requested by the participants. The members of the Group countries (those representatives were usually senior civil servants of member countries of GATT) were responsible for hearing cases of trade policy, and met three or four times a year to examine some of the major commercial policy issues of the day. The Chairman of the Group presented a report to the Council every year which was taken up in the Council's report sent to the Contracting Parties. The Group was given the task of facilitating the carrying out of the responsibilities of the Contracting Parties, particularly with respect to the aspects: "(a) following international trade developments with a view to the pursuit and maintenance of trade policies consistent with the objectives and principles of the General Agreement; (b) the forestalling, whenever possible, of sudden disturbances that could represent a threat to the multilateral trading system and to international trade relations generally; and action to deal with such disturbances if they in fact occur; (c) the international adjustment process and co-ordination, in this context, between the GATT and the IMF".¹⁹

Dispute Settlement and Surveillance adopted 28 November 1979, L/4907, BISD 26S/210.

¹⁶For the list of GATT panellists, see Pescatore Pierre, William J. Davey and Andreas F. Lowenfeld, Handbook of GATT Dispute Settlement [hereinafter, the "Handbook"], Transitional Juris Publications, Inc., New York, 1991 (the Release 8 was June 1997), pp. Index 4/1-4/3.

¹⁷BISD 22S/15.

¹⁸BISD 26S/289.

¹⁹For discussion on establishment of the Consultative Group of Eighteen (CG-18), C/M/107,

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The restricted membership of the Group allowed it to work more efficiently. It had a consultative nature, and whenever a consensus emerged within the Group (which had a balanced and representative membership as far as nationalities were concerned) this consensus was likely to be repeated and find expression in the Council and at the sessions of the Contracting Parties.

In the Forty-fifth Session in December 1990, the DG made a suggestion to the Council that the Group be suspended and the CP so agreed. In fact, the Group was not convened during the next two years.

1.1.5. The Director-General²⁰

As defined in the provision of the Havana Charter, the DG was supposed to be the chief administrative officer of the ITO. The title of the DG came into being by virtue of the Decision of 23 March 1965.²¹ In 1957, the Executive Secretary took over the functions of the Secretary-General of the United Nations, the institution which was also the depository of GATT instruments as stated in the text of the General Agreement. In practice, the Executive Secretary continued to have responsibility for certain functions under the General Agreement, while the DG held the position of chief administrative officer of the Organisation. To put an end to such an awkward situation, powers and duties were conferred on the Executive Secretary by the General Agreement as provided in the Decision of 23 March 1965,²² which stated that such powers and duties "shall be exercised by the person holding the position of DG who shall for this purpose also hold the position of Executive Secretary".²³ In fact, there was no definition as to the powers and scope of the mandate of the DG in

BISD 22S/15-16; for revised mandate, **BISD 26S/289-90**. Reports made by the CG-18 can be found at **BISD 25S/37**; **BISD 26S/284** and others.

²⁰There have been five different Director-General of GATT up to now: Sir Eric Wyndham White (1948 - 1968); M. Olivier Long (1968 - 1980); M. Arthur Dunkel (1980 - 1993); Peter Sutherland (1993 - April 1995); and Renato Ruggiero who currently takes the position (1 May 1995 - expected to end his term at the end of April 1999).

²¹**BISD 13S/19**.

²²*Ibid.*

²³*Ibid.*

the General Agreement. His functions had developed empirically, influenced mainly by the actions of the successive appointees to the post. The main duty of the DG was to act as negotiator, and to chair the trade negotiation committees. The idea behind this role was that the independent position of the DG guaranteed impartiality when the parties were holding negotiations in which different national interests were at issue. Furthermore, the DG held consultations and informal negotiations with the objectives of the avoidance of trade disputes and the promotion of peaceful solutions to differences existing between parties, and also in an attempt to reach consensus among contracting parties on all matters. The DG, however, had no legal rights of enforcement and thus he relied mainly on his personal capacity of persuasion.

1.1.6. The Secretariat

There was no reference to a GATT Secretariat in the General Agreement.²⁴ Originally, the Interim Commission for the ITO (hereinafter, the "ICITO") provided secretariat services for GATT.²⁵ The function of the ICITO survived the failure of the ITO, and developed empirically. The term "GATT Secretariat" appeared in the multilateral trade agreements reached in the Tokyo Round. The Secretariat of GATT was divided into three major departments as well as the Director's office and the International Trade Centre. Those departments were: (1) the Department of Conference Affairs, Liaison and Administration; (2) the Department of Trade Policy; and (3) the Department of Trade and Development. The Secretariat was presided over by the DG.²⁶ Furthermore, the role of the Secretariat was prescribed in the following documents:

- paragraph 6 (iv) of the 1979 Understanding Annex;
- paragraph (iv) of the 1982 Ministerial Decisions;

²⁴ Cf. The Secretariat is defined formally under the Article VI of the **Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations**; see, MTN/FA II, pp. 3-4.

²⁵ See Jackson, J. H., The Law of GATT, *supra* note 6, pp. 49-50 and 145-147.

²⁶ Until 1965, the Director-General was referred to as the "Executive Secretary", see, the Decision of 23 March, 1965, **BISD 13S/19**, *supra* note 21; see also, Jackson, The Law of GATT, *supra* note 6, pp. 148-150.

- the reference in paragraph H.1 of the 1989 Improvements; and
- provisions of technical assistance to developing contracting parties.

1.2. Objectives of GATT

The aim of GATT can be found in its Preamble:

[...] with a view to raising standards of living, ensuring full employment and a large and steadily growing volume of real income and effective demand, developing the full use of the resources of the world and expanding the production and exchange of goods²⁷

The founding contracting parties of the GATT committed themselves to the principle of *non-discrimination* in their trade relations in order to ensure equal access to markets and *reciprocity* in trade concessions. Again, in the Preamble to the General Agreement, their commitment was stated as follows:

The contracting parties are desirous of contributing to these objectives by entering into reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade and to the elimination of discriminatory treatment in international commerce.²⁸

These objectives of the General Agreement were refined by the addition of GATT Article XXXVI to Part IV of GATT which became effective on 27 June, 1966.²⁹ This additional article came into being as a result of new circumstances that emerged in the developing countries, which could not be satisfied by the original provisions, for instance, GATT Article XVIII (Government Assistance to Economic Development). According to GATT Article XXXVI, the contracting parties recognised that the basic objectives of GATT included the raising of standards of living and the progressive development of the economies of all the contracting parties and considered that the attainment of these objectives was particularly urgent for the less-developed member states. The contracting parties noted that there was a considerable gap between the standards of living in less-developed countries and

²⁷ GATT, the Preamble to the General Agreement on Tariffs and Trade (GATT 1947).

²⁸ *Ibid.*

²⁹ The Protocol Amending the General Agreement on Tariffs and Trade to Introduce a Part IV titled Trade and Development, which was done on 8 February 1965 and entered into force on 27 June 1966, BISD 13S/2.

those in other countries. To bridge this gap, the contracting parties recognised that individual and joint action was essential to further the development of the economies of less-developed countries and they acknowledged the need for affirmative discrimination in favour of less-developed countries.

1.3. The Structure of the Agreement

The GATT text consisted of four parts:

- The first part (Article I and II): dealt with the general treatment of Most-Favoured-Nation (MFN) and its consequences or of concessions provided for in GATT;
- The second part (Article III to XXIII): spelled out the substantive rights and obligations of the contracting parties under GATT;
- The third part (Article XXIV to XXVIII): defined what was to be understood as implementation and procedures; and
- The fourth part (Article XXXVI to XXXVIII): dealt with the special position of those less-developed countries under the system.

In addition, nine annexes alphabetised (A to I) had been attached to the GATT text: Annex A to G covered the issue relating to Article I; Annex H dealt with the issue relating to Article XXVI; Annex I was titled Notes and Supplementary Provisions. They formed an integral part of GATT, as did the Schedules.³⁰ In practice, a number of separate agreements had been concluded under GATT and those agreements were able to introduce changes to rights and obligations or elaborate them in further detail.

³⁰ Article II: 7.

1.4. Main Legal Principles³¹

Although the GATT and its associated agreements contained a number of complicated rules, these were all, however, based on a set of relatively few principles and objectives. Furthermore, in fact, those main legal principles of GATT have been carried on to the WTO system. Major principles are briefly demonstrated in turn.

1.4.1. The Principle of Reciprocity³²

Reciprocity can be defined as the maintenance of balance in any trading relationship, where access to the domestic market of one country is exchanged for access to the other and mutually agreeable rules of fair trade are established.³³ When the GATT was established in 1948, the concept of reciprocity was included in the GATT because of U. S. pressure. Accordingly, the GATT embodied the principle of reciprocity in the form of a mutually beneficial clause, where signatory countries were to expect equal treatment abroad for their producers in exchange for what they could offer to the producers of other nations. In addition, the principle of reciprocity also existed as a means of enforcing a fair treatment and mutual benefit, i. e., if a country fails to observe the trade rules stipulated in the GATT, any other country adversely affected by that behaviour may retaliate to restore the balance in their trade relationship.³⁴

Reciprocity, for instance, was an important instrument in the reduction of tariff barriers. Reciprocity as a legal concept had not been defined by the Contracting

³¹ See, *supra* note 1; Supervisory Mechanisms in International Economic Organisations, Kluwer Law and Taxation Publisher, Deventer, The Netherlands, 1984, pp. 58 ff.

³² See, generally, Jackson, J. H., The World Trading System [hereinafter, the "World System"], 2nd ed., The MIT Press, Cambridge, Massachusetts 1997; GATT, Analytical Index: Guide to GATT Law and Practice [hereinafter, the "Analytical Index"], 6th ed., 1994; and Rhodes, Carolyn., Reciprocity, U.S. Trade Policy, and the GATT Regime [hereinafter, the "Reciprocity"], Cornell University Press, Ithaca, U. S., 1993, especially Chapter 1 and 4.

³³ Keohane notes that "*reciprocity refers to exchanges of roughly equivalent values in which the actions of each party are contingent on the prior actions of the others in such a way that good is returned for good and bad for bad.*", see Keohane, Robert O., "Reciprocity in International Relations", 40 International Organisation (Winter 1986) at 8.

³⁴ *Ibid.*

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Parties, but was nevertheless a fundamental principle in the General Agreement whose importance was stated clearly in the Preamble.³⁵ Pursuant to GATT Article XXVIII: 2, the negotiations on tariffs were to be held on a reciprocal and also mutually advantageous basis in order to attain a substantial reduction in the general level of tariffs. This objective, unfortunately, could not always be achieved. For example, the value of whatever concessions were made was not always easy to quantify, particularly when non-tariff concessions were part of the equation. The concessions set by socialist countries, for example, usually consisted of commitments to increase imports. Nonetheless, these were hardly comparable with tariff concessions provided for by western countries. Moreover, countries with a high tariff rate, had a more advantageous position than those with low tariffs.³⁶ This illustrates the fact that developing countries, with their low national income, and therefore low imports,³⁷ could afford to offer little, if anything, in exchange for concessions from other countries. Accordingly, developing countries needed concessions from bigger trading partners in order to increase their exports which were essential for their economic development. In addition to those difficulties, developing countries were not always able to offer concessions because of the unfavourable situation of their balance-of-payments and the necessity to protect newly established (or infant) industries. Accordingly, this principle was difficult to apply and what in theory appeared to be fair, in practice, could be unjust since the lack of real equality between countries hindered its use in the bargaining process.³⁸

Therefore, to overcome those difficulties, the General Agreement offered a number of means by which to secure real reciprocity between trading partners, for example, anti-dumping duties, the compensation, suspension of concessions or other obligations provided for in GATT Article XXIII, nullification and impairment and others. To that end, contracting parties were supposed to use those provisions to

³⁵ See, *supra* note 27.

³⁶ See, K. W. Dam, The GATT Law and International Economic Organisation, Chicago Univ. Press, 1970, p. 59.

³⁷ According to the general macro-economic theories, imports are mainly a function of the national income.

³⁸ See, Jackson, J. H., The Law of GATT, *supra* note 6, pp. 242-245.

secure compensation or apply retaliatory actions to restore balance to their trade relationships. Nevertheless, those actions might be in violation of the principle of MFN treatment.

1.4.2. The Principle of Non-Discrimination: The Most-Favoured-Nation Treatment³⁹

Most-Favoured-Nation treatment was one of two aspects of the principle of non-discrimination provided for in GATT Article I. The article prescribed the use of the MFN in trade relations between the contracting parties:

[...] any advantage, favour, privilege or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all contracting parties.⁴⁰

The principle meant that if one country granted to another country MFN treatment, it must immediately and unconditionally extend the same treatment to the rest of the member countries. However, the MFN treatment embodied in GATT was subject to a number of exceptions. For example:

- Regional integration agreements were exceptions to the MFN clause. (e.g. GATT Article XXIV which dealt with the creation of customs unions and free-trade areas.)
- Exceptions or waivers approved by the CONTRACTING PARTIES on an *ad hoc* basis. (e.g. GATT Article XXV:5 which stated the Contracting Parties could authorise non-compliance with a GATT obligation by a member state.)
- General exceptions and/or security exceptions were also available, for example, GATT Article XX which mentioned the aspects of public policy, and under GATT Article XXI which covered security aspects.⁴¹

³⁹ See, GATT, *The Analytical Index*, *supra* note 32; Jackson, J. H., *The World System*, *supra* note 32.

⁴⁰ GATT Article I, para. 1.

⁴¹ See e.g., In 1982, member countries imposed an embargo on Argentine imports at the time of the Falklands - Malvinas conflict.

-The historical preference, also known as the "grandfather clause" in preferential arrangements was exempted. (e.g. GATT Article I:2, 3 and 4 which maintain preferences between former colonies and its sovereign countries. This treatment was needed at the time when the GATT came into effect.)

1.4.3. The Principle of Non-Discrimination: The National Treatment⁴²

As already mentioned, the MFN principle of GATT required countries not to discriminate among GATT contracting parties. The principle of national treatment of GATT was the other aspect of the principle of non-discrimination and also complementary to the MFN principle. According to GATT Article III in which national treatment was stipulated, the products of any member country imported into any other member were treated, as far as any internal tax, charges or regulation were concerned, on the same condition as like domestic products. GATT Article III applied to all kinds of taxes and internal charges, and therefore, it concerned laws, regulations and requirements that affected the internal sales, purchase, transportation, distribution or use of products available on the domestic market. In other words; the principle of national treatment required countries not to discriminate between domestic products and imported products by giving less-favourable treatment to the latter. Hence, national treatment granted to imported products in this way provided a defence against protectionism resulting from internal administrative and legislative measures. Nevertheless, as for customs duties and other border measures (e.g. inspections of health safety standards, etc.), these were outside the scope of these provisions.

1.4.4. Other Principles

Apart from the essential principles indicated above, there were other principles which provided for procedures to enhance the liberalisation of trade, fair competition, and

⁴² See, GATT, *The Analytical Index*, *supra* note 32; Jackson, J. H., *The World System*, *supra* note 32;

developing world trade based on multilateral negotiation. To that end, the GATT opposed, for instance, tariff restrictions (e.g. customs duties), quantitative restrictions (e.g. export licence, quotas) and the rest of the Non-Tariff Barriers (NTBs) (e.g. a number of protective measures⁴³).

1.5. Preference⁴⁴

A contracting party had to give preference, which meant giving exemptions to the GATT rule, to developing countries in a number of cases. On the face of it, this practice was in conflict with the principle of reciprocity and with that of MFN treatment. In 1958, Article XXVIII *bis*: 3(b) was added to the GATT. That article required the contracting parties to take due consideration of the needs of less-developed countries, and to apply favourable treatment as regards tariff protection so as to assist in their economic development and also to cater for their special needs to maintain tariffs for revenue purposes. In addition, since the introduction of GATT Article XXXVI:8 in 1966, developed contracting parties should no longer expect reciprocity for commitments made by them in trade negotiations to reduce or remove tariffs and other barriers to the trade with less-developed contracting parties. Pursuant to GATT Article XXXVII:1(a), developed contracting parties had to accord a high priority to the reduction and elimination of barriers to trade with less-developed contracting parties. Moreover, on 28 November 1979, the GATT member states adopted an agreement entitled "Differential and more favourable treatment, reciprocity and fuller participation of developing countries",⁴⁵ also referred to as the "Enabling Clause".⁴⁶ This agreement

⁴³ See, Jackson, J.H., *The World System*, *supra* note 32, pp. 154-155; see also Jackson, J.H. and William J. Davey, *International Economic Relations*, 3rd ed., West Publishing Co., St. Paul, 1995, pp. 377-378.

⁴⁴ GATT, *The Analytical Index*, *supra* note 32.

⁴⁵ BISD 26S/203-205 (1980); for the "Enabling Clause", see *The Analytical Index*, *supra* note 32; The background of the enabling clause is follows: the General System of Preference (GSP) programme is to provide less developed countries with a certain trade favour (in the form of special and differential treatment), which was operated under the benefit of a waiver from GATT MFN Principle from 1971 through to 1981, see Decision of 25 June 1971, L/3545 in BISD 18S/24-26 (1972). In addition, this programme was amended and authorised by the "enabling clause" under the Tokyo Round Understanding (1979) [officially

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continued the tradition of providing developing country members with more favourable treatment. Furthermore, under this agreement, the least developed countries were given special treatment in spite of the MFN provisions of GATT Article I under the non-discrimination principle. In this respect, adoption of the Enabling Clause could be seen as legalisation of the philosophy of preferential treatment in trade relations among contracting parties with different economic levels.

named "Differential and More Favourable Treatment, Reciprocity, and Fuller Participation of Developing Countries", see Decision of 28 November 1979, L/4903 in **BISD 26S/203-205 (1980)**]; see in general Yusuf, "Differential and More Favourable Treatment: The GATT Enabling Clause", 14 J.W.T.L. (1980), pp. 488-507; also see Balassa, "The Tokyo Round and the Developing Countries", 14 J.W.T.L. (1980), pp. 93-118; and for an overview of the history of developing countries under GATT up to WTO, see Hoekman, Bernard., and Michel Kostecki, The Political Economy of the World Trading System: From GATT to WTO, Oxford University Press, Oxford, 1995 at pp. 323-245.

⁴⁶ See, *supra* note 1.

Chapter 2. GATT DISPUTE SETTLEMENT MECHANISM¹

"GATT members have the dispute settlement process they deserve. It works surprisingly well in most places where they want it to work - and does not work where they do not want it to".²

Introduction

In the previous chapter, we dealt with the GATT and its legal order. This chapter analyses, the dispute settlement system of GATT, one of the most important as well as controversial issues of the GATT. A large number of defects in the system became urgent issues requiring to be improved and overcome from the early 1950's until the recent establishment of WTO. Furthermore, perceptions of the effectiveness and even the usefulness of the system have varied over the years, which, for instance, depended on the economic performance of each contracting party.

This chapter will first look at the "old" dispute settlement system under the GATT legal order, then identify problematic issues within this dispute settlement system and, in the end, examine a number of changes and/or developments introduced to it in order to resolve the outstanding defects in the dispute settlement system and further improve the system.

¹ See, Pescatore, Pierre., "The GATT Dispute Settlement Mechanism - Its Present Situation and its Prospects", 27 J. W. T. (1993), pp. 5-20.

² Plank, Rosine., "An Unofficial Description of How a GATT Panel Works and Does Not", 29 Swiss Rev. Int'l Competition L. (1987) at 123.

2.1. Outline of the GATT Dispute Settlement History³

2.1.1. The First Decade (1950s)

During the initial decade from 1948 to 1959, the GATT dispute settlement system was quite successful, and functioned relatively well. This can be attributed to a number of factors. First, the General Agreement had only recently been negotiated at that stage and there was a general consensus on what it meant and how it should be interpreted.⁴ Second, the number of GATT members was rather limited, starting with 23 countries in 1948, and their backgrounds and trade policies aiming at lowering barriers (i.e. tariffs, non-tariff barriers) to international trade were relatively similar.⁵ Furthermore, many of the GATT diplomats dealing with GATT matters during this period had participated, in person, in the creation of the system and probably had a greater stake in contributing to its success.⁶ In this period, 53 disputes between member states were brought to GATT. Meanwhile, GATT introduced a new system called "panel proceedings" for adjudicating legal disputes.⁷ This mechanism was an informal process and more diplomats than lawyers were engaged as judges who were

³ For a useful chronological study on GATT dispute settlement conducted by Professor Hudec and this section is partly based on his survey, see Hudec, Robert E., Enforcing International Trade Law: The Evolution of the Modern GATT Legal System [hereinafter, the "Enforcing Trade Law"], Butterworths Legal Publisher, New Hampshire, U. S., 1993.

⁴ See, Hudec, R. E., Adjudication of International Trade Disputes (Thames Essay No. 16), Trade Policy Research Institute, London, 1978, pp. 14-21.

⁵ *Ibid.*, at 14, 21-23.

⁶ See, Hudec, R. E., The GATT Legal System and World Trade Diplomacy, Praeger Publishers, New York, 1975.

⁷ With respect to this change, from working parties to panels, can be found at Sections 1.1.3.2. and 1.1.3.3. in Chapter 1 of this thesis; The panel procedure was adopted at the Seventh Session in 1952. In general, this procedure was almost the same as the present one. However, unlike the present panel, the representatives of disputing parties could also be a member of the working party in which a disputing issue is ruled; cf. "the Committee [Australia, Belgium, Brazil, Canada, Chile, Cuba, Denmark, France, Germany, India, Italy, Pakistan, the Union of South Africa, the United Kingdom and the United States] may establish a working party consisting of some or all of its members, together with the countries directly concerned, any countries which claim a substantial interest in the matter and which wish to be represented on the working party, and any other countries which the Committee may consider it necessary to invite and which are willing to serve" in **BISD 1S/7 (1953)**; In addition, the first appearance of the term, "panel", was at the Ninth Session in 1955; cf. "(...) the appointment of qualified panels to assist in carrying out consultations (...) and in the consideration of complaints under Article XXIII, (...)", see at para. 52, **L/327 in BISD 3S/247 (1955)**.

called "panellists". The legal rulings were drafted with a diplomatic approach; in other words, it was based on a "pragmatic" or "power-oriented" (i.e., more politically-oriented) approach.⁸ During this period, Japan became a GATT contracting party acquiring full membership when it joined on 10 September 1955.

2.1.2. The Second Decade (1960s)

During the 1960s, the membership of GATT increased and the world economy expanded rapidly. In particular, the developing countries' membership increased to a numerical majority which enabled them to act *en bloc* on several occasions. On the other hand, with respect to the developed countries, membership was radically altered by the formation and subsequent enlargement of the EEC, what is now generally referred to as the European Community (hereinafter, the "EC") along with the emergence of Japan as a major economic power. Thus, whatever "easy" consensus was available in the previous decade, it collapsed in the 1960s due to an increase in the complexity of the conflicts within the GATT and the emergence of two "new" members, that is, the European Community and developing countries bloc. In this period, the dispute settlement system of GATT was still based more on a "power-oriented" approach than on a "rule-oriented" one.

There were two major factors for the decline of the previous "consensus". First, the creation of the EC caused a change as regards the European countries. The original six states of the EC (i.e. France, West Germany, Italy, the Netherlands, Belgium and Luxembourg) were the founding members (23 countries) of the GATT. In the 1960s, the EC no longer relied on the dispute settlement system of GATT. The EC acted as one body in dealing with international trade issues and relevant negotiations instead of dealing with them individually (relatively smaller member states).⁹ The second reason was the expansion of the number of members from the developing countries

⁸ See, Jackson, J. H., The World Trading System, 2nd ed. The MIT Press, Cambridge, Massachusetts, 1997, pp. 109-111.

⁹ See, for the Common Commercial Policy Swann, Dennis., The Economics of the Common Market, 6th ed., Penguin Books, London, 1988 (reprinted in 1990) at 298.

as contracting parties. Incidentally, the balance of membership of the contracting parties between developed and developing countries shifted from 21:16 (1960) to 25:52 (1970).¹⁰ In the meantime, the developed country members achieved their main goals of tariff reduction and removal of their own balance-of-payments restrictions during this decade.

The EC claimed the right to be exempt from the GATT provisions in the areas of agriculture¹¹ and in other aspects, for example, those involving their commercial relations with former colonies in Africa, the Caribbean and the Pacific (hereinafter, the "ACP")¹². During this period, EC policy was based more on the "diplomatic" approach to dispute settlement instead of the "rule-oriented" (i.e., the use of the GATT law including its dispute settlement mechanism). Likewise, the United States followed a similar attitude of "anti-legalism", at least during the period from 1963 to 1970. Those two leading economies regarded formal claims by other GATT members as "legalistic", accompanied by the introduction of the notion that such legal claims were seen as "unfriendly actions".

Accordingly, an anti-legalist position prevailed during this period, and eventually the GATT system was suspended and undermined. Both the U.S. and the EC did not seem comfortable with the possibility of submitting themselves to an adjudicatory ("rule-oriented") system which became gradually more explicit in GATT. Ironically, their preference for a non-judicial approach was motivated by their concern over losing their "political" control or influence over the system which they had created.

2.1.3. The Third Decade (1970s)

This period stretches from 1970 to the 1979, being notable as the period in which the Tokyo Round of negotiations took place. This was also the period when GATT began to rebuild its legal system. The need for rebuilding the GATT system was

¹⁰ See, BISD 8S/99 (1960); BISD 17S/ vii (1970).

¹¹ See, for the Common Agricultural Policy [hereinafter, the "CAP"], *supra* note 9, pp. 205-231.

¹² See, for the ACP countries, *supra* note 9, pp. 301-304.

initiated by the United States because domestic political developments created a demand for stronger enforcement of U. S. trade agreement rights. The main point in the legal rebuilding of the system was the negotiation of several new "MTN Codes" covering Non-Tariff Barriers (hereinafter, the "NTBs").¹³ With respect to the dispute settlement, the new code rules required a strong dispute settlement procedure to make them reliable, and each code contained its own dispute settlement procedure. The number of disputes during this period was 32 even before the 1979 reforms were adopted. Thus, by the end of the period, dispute settlement had recovered its legal orientation. In short, the popular approach to resolving disputes became more rule-oriented.

2.1.4. The Fourth Decade (1980s)

In the 1980s, the GATT legal system became increasingly complex but, at the same time, it was often referred to when disputes arose between contracting parties. The governments of the GATT members filed 115 legal complaints in this period, of which 47 (40%) were finalised by panels. These figures should be seen as the landmark of the new era. Indeed, the tremendous increase of cases brought to the GATT forced the GATT Secretariat to create a legal office which was finally set up in 1983.¹⁴ There were, however, unsuccessful cases due to the excessive political pressure or demands placed by member state governments. In short, the "political" approach was very much alive. One of the main causes of mal-function of the GATT system was that contracting parties tended to use their veto power under consensus in

¹³The NTBs are government measures other than tariffs that restrict trade flows. For example, quantitative restrictions, import licensing, voluntary restraint arrangements and variable levies. They generally now contravene the WTO rules (this definition is from Goode, Walter., Dictionary of Trade Policy Terms, Centre for International Economic Studies, University of Adelaide, Australia, 1998 at pp. 199-200); see also, Jackson, J. H., *supra* note 8 pp. 75-78.

¹⁴Moreover, the creation of the Legal Affairs Office at the GATT Secretariat was also propelled by the lesson learnt from the DISC case in which the EC claimed the U.S. concerning its 1971 Income Tax Legislations (DISC), for this case L/4422 (2 November 1976), BISD 23S/98-114 (1977), for a problem and contribution from the DISC case, see Hudec, Robert. E., Enforcing International Trade Law: The Evolution of the Modern GATT Legal System, Butterworths Legal Publishers, New Hampshire, 1993 at pp. 99-100.

the decision-making practice of blocking the creation of panels or the adoption of adverse panel reports.

In the meantime, an anti-legalistic hostility to the policy of the GATT was once again growing in the United States; certain groups in the United States claimed that GATT law was not effective enough to protect U. S. national interests.¹⁵ Furthermore, the trade deficit of the U. S. during the mid-1980s strengthened the GATT sceptics in the United States even more. A very important American development of the period was the emergence of what is called "unilateralism", which appeared in the form of Section 301 of the Trade Act 1974.¹⁶ This questionable policy imposed demands, unilaterally, on governments which allowed room for illegal or "unreasonable" restrictions. It then demanded correction under the threat of trade retaliation, which was frequently illegal under the GATT. Paradoxical though it might seem, one of the initial promoters of strengthening GATT law, the United States, yielded to domestic pressures and introduced legislation which clearly undermined the law of GATT. The U. S. appeared to be willing to turn the clock back so as to halt the process of GATT legal reform.

2.1.5. The Fifth Decade (Until 1994)

In general, this period can be characterised as the period of "inactivity" or "wait and see". This paralysation of the system happened mainly because of the then ongoing Uruguay Round (hereinafter, the "UR") negotiations. The contracting parties were concerned about the outcomes of the negotiations. Due to such uncertainty over the future of the GATT system, the contracting parties deferred filing reports until they learned about the outcome of the negotiations. Even the GATT panel which was established to deal with certain disputes delayed in making decisions. In addition,

¹⁵ Hudec, R.E., The Enforcing Trade Law, *supra* note 3, at pp. 107-111.

¹⁶ See, Jackson, J. H., Restructuring of the GATT System, Royal Institute of International Affairs, London, 1990, pp. 69-73; Jackson, J. H. , & William. J. Davey, Legal Problems of International Economic Relations: cases, materials and text [hereinafter, the "Int'l Econ. Relations], 3rd ed., West Publishing Company, St. Paul, Minnesota, 1995.; Bhagwati, Jagdish. and Hugh T. Patrick (eds.), Aggressive Unilateralism - America's 301 Trade Policy and the Trading System, Haverster Wheatsheaf, U. K. , 1991.

the Contracting Parties also put off voting on the adoption of the panel reports. In fact, this unfortunate trend was noted by the Mr. Peter Sutherland, the DG at that time, in his report to the Council on 10 November 1994.¹⁷ To sum up, none of the functions of the dispute settlement mechanism were in order during this period.

2.2. The Old Procedure of GATT Dispute Settlement

The old GATT dispute settlement procedure lacked uniformity. On one hand, there was a general system of conciliation and dispute settlement based on Articles XXII and XXIII of the General Agreement. These two articles emphasised bilateral consultation as a first step in settling disputes. On the other hand, a variety of specific dispute settlement procedures were provided for in different codes in most of the Tokyo Round agreements.¹⁸ Each Tokyo Round agreement, with the exception of "Import Licensing", had its own mechanism for dispute settlement which was separate from the "general" dispute settlement procedure of the General Agreement. In addition to those various dispute settlement procedures, developing countries were also entitled to special rules of procedure.¹⁹

The general dispute settlement procedure of GATT, provided for in Article XXII and XXIII, had three aims: the realisation of GATT's purposes, the protection of the benefits accruing under the General Agreement, and dispute settlement. Actions could be taken in cases where the purpose of GATT was violated even when no formal GATT provisions have been contravened (i.e. a non-violation claim under Article XXIII:1(b)). Moreover, violations could be legalised if necessary by means

¹⁷ During the past 12 months compared with the previous 12-month period: the number (no.) of consultations (from 31 to 15); the no. of panels established (from 7 to 4); the no. of panel reports adopted (from 4 to 3); and the no. of disputes in which implementation issues were raised (from 10 to 2), for the status of active dispute settlement in GATT, see GATT Focus No. 112 (November 1994) at 4-5.

¹⁸ See, Jackson, J. H. & W. J. Davey, *supra* note 16, pp. 379-391; also for general information, see, **BISD S26 (1980)**.

¹⁹ See, for instance, the 1979 Understanding (dealt in Section 2.4.1.5.), paras. 5, 6(ii), 8, 21 and 23; the 1966 Procedures (dealt in Section 2.4.1.3.); the 1989 Improvements (dealt in Section 2.5.2.), para. 7 of Section F(f), para. 1 of Section H, and para. 4 of Section I.

of a waiver by the CPs (i.e. Article XXV:5), which permitted deviation from GATT obligations.

2.2.1. The Dispute Settlement Process Set Out in Article XXII and XXIII

GATT Article XXII: 1, required consultation with respect to "any matter affecting the operation" of the General Agreement. If such bilateral consultations were unsuccessful, Article XXII: 2 of GATT, provided for the possibility of setting up a Working Party or Panel,²⁰ open to all GATT members, including of course disputing parties.

Article XXIII: 1, provided for bilateral consultations whenever a "nullification or impairment" of a GATT benefit or an impediment to attaining a GATT "objective" was alleged. If no mutually satisfactory solution was reached, Article XXIII: 2, provided for the matter to be investigated by the CP, who could make recommendations or give a ruling. It was in this context that the practice had developed of setting up a panel to assist the CP. On the other hand, however, the substantial function of Article XXIII: 2 procedures had been to provide an incentive to settle disputes by mutual agreement.

Although no provisions for panels were made in Article XXIII: 2, the practice of creating panels had grown through customary practice in connection with the continued implementation of the Article. The practice of creating panels was finally codified at the Tokyo Round under the "Understanding Regarding Notification, Consultation, Dispute Settlement and Surveillance", adopted on 28 November, 1979.²¹ In addition, a postscript was attached named "Agreed Description of the

²⁰For more information, see at Sections 2.1.3.2. and 2.1.3.3. in Chapter 2 of this thesis; see also *supra* note 7.

²¹**Understanding Regarding Notification, Consultation, Dispute Settlement and Surveillance, Document L/4907, BISD S26/210 (1980)**, [hereinafter referred to as the "1979 Understanding"]. The 1979 Understanding mainly summarised the procedures of dispute settlement that had been used in GATT and indicated that they would continue to be used. The 1979 Understanding, however, made no significant changes in GATT dispute settlement procedures except for specifying certain limits in which various actions ought to be taken. It was noteworthy because it indicated that cps were willing to maintain the system they had developed.

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Customary Practice of the GATT in the Field of Dispute Settlement (Article XXIII:2)" to the 1979 Understanding.²² In fact, there was no transparent and detailed procedures for dispute settlement until the installation of the 1979 Understanding despite the general procedures provided for in Article XXII and Article XXIII of GATT. The purpose of this Understanding was to support the parties in settling their disputes. It illustrated the combination of law and diplomacy which co-existed in the dispute settlement system, as was the case of the GATT system itself. In general, it has been observed by the majority of contracting parties that this was the secret of reasonable success which had been achieved during the era of GATT.

Pursuant to Article XXIII: 2, if bilateral consultations failed to resolve the matter in dispute regarding the practice concerned, the complainant was to notify the CP that it wished to bring the issue in dispute before them. A request for a panel of independent experts was always granted although there was no provision for the automatic setting up of panels.

The composition and terms of reference for a panel was, in principle, to be determined within 30 days following the decision of its establishment. In practice, however, it took much longer. This was partly because the panel members, usually 3 or 5, had to be agreed on by the parties to the dispute. In addition, these panel members were selected from members of the delegation in Geneva, and as a result there were more civil servants than lawyers.²³

The task of a panel was to prepare a report to the CP "to assist" them "to deal with the matter".²⁴ This report was required to include "an objective assessment of the matter before it, including an objective assessment of the facts of the case and applicability of and conformity with the General Agreement."²⁵

²² See, *ibid.*, Annex, *supra* note 21, especially paras. 3 and 6.

²³ See, Plank, Rosine., "An Unofficial Description of How a GATT Panel Works and Does Not", 29 Swiss Rev. of Int'l Competition Law (1987), p. 81, 91-97.

²⁴ *Ibid.*, *supra* note 21, para. 10.

²⁵ *Ibid.*, *supra* note 21, para. 16.

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Once a panel was appointed, its task was normally to examine the dispute and make such findings as would assist the CP in making recommendations or rulings as provided for in Article XXIII.²⁶ The panel received written and/or oral submissions from the CP and might also receive submissions from other interested parties. The panel might request from the CP any information which it deemed "necessary and appropriate" and answers should come "promptly and fully" from any cp. In addition, the panel might seek information and technical advice from any individual or body within the jurisdiction of a State, after informing the Government of that State.²⁷

The panel was assisted by the GATT Secretariat which provided the secretary to the panel. The secretary provided by the Secretariat not only prepared the summary of the proceedings, but also engaged in research and drafted the panel report. Before releasing its final report to the CP, the panel had to submit the descriptive parts of its report to the parties concerned together with the panel's conclusions and recommendations. The purpose of this exercise was to encourage a development of mutually satisfactory solutions between the parties to a dispute as well as obtaining their comments (as we shall see in Chapter 5, this practice still exists under the new rules of WTO, i.e. DSU 15). The parties were given a reasonable time, normally from one to two months, to examine the report and discuss the possibility of settling their dispute. If it was not resolved before such a deadline, the panel circulated its report to all cps as a GATT document, which would then be included in the agenda of the following Council meeting.

The panel report, however, had no legal force and had merely the status of an "advisory opinion".²⁸ It had to be adopted first by the Council on behalf of the CP. The Council usually adopted the report as it was. This adoption was decided on the basis of consensus. There was always the possibility that the losing party could

²⁶ Panel procedures are summarised in, *supra* note 21.

²⁷ *Supra* note 21, para. 15.

²⁸ Annex, *supra* note 21, para. 6(i).

prevent adoption of the report in the Council.²⁹

During the period from 1948 to 1986, 100 complaints were brought under Article XXIII: 2; out of those complaints, 52 led to the submission of a report by a panel. The others were settled without a report; of the 52 reports, 50 (96%) were adopted or led to a mutually satisfactory solution and a withdrawal of the complaint, and were implemented without adoption; the reports of the remaining two cases have not resulted in either of the disputes being settled.³⁰

As to compliance with the recommendations adopted by the Council, the 1979 Understanding provided that the CP would keep under surveillance any matter on which they had made recommendations or given rulings. If the CP's recommendations were not complied with within a reasonable period of time, the successful petitioner might ask the CP to make suitable efforts with a view to finding an appropriate solution.³¹

In the event of non-implementation, provided for in Article XXIII: 2 of GATT, the CP might authorise the injured party to suspend the application of concessions or other obligations under the General Agreement to the party which had failed to comply (i.e. in fact, this meant "retaliation" but expressed in a diplomatic manner).³² There was only one case in which this right to retaliate had been invoked and authorised.³³

²⁹The 1982 Ministerial Declaration stated, "*The Contracting Parties reaffirmed that consensus will continue to be the traditional method of resolving disputes; however, they agreed that obstruction in the process of dispute settlement shall be avoided.*", see the 1982 Declaration, *infra* note 39, para. 10.

³⁰See, GATT, GATT Focus, No. 46 (May 1987) at 2.

³¹*Supra* note 21, para. 22. (cf. Under the DSU of the WTO, "Surveillance" is defined under Article 21).

³²Annex, *supra* note 21, para. 4. (cf. DSU 22)

³³In 1952 the Netherlands was authorised to impose a discriminatory quota on imports of

2.3. The Main Defects of the GATT Dispute Settlement System

2.3.1. Access to the Procedure

The right to file a complaint was restricted to a country who had a direct and substantial interest in the matter. Nonetheless, in the case of a small country (in economic terms), it sometimes took them some time to decide to initiate action against a large and economically powerful country due to the limitation in its economic and political bargaining power.

2.3.2. The Panel Process

There were a number of specific problems concerning the operation, status and circumstances of panels. In particular, those problems could arise from factors such as lack of expertise, neutrality, and even quality in panel reports. First of all, panels were usually composed of persons with no previous panel experience, and many had none of the expected expertise to discharge the function as a panellist. This problem became more serious when the dispute involved the major influential countries such as the U.S. and the EC because more experts were from those countries. When panellists were selected from smaller countries, another problem appeared; the country from where those panellists were selected often heavily relied on the major economies. Second, there was the problem of the neutrality of panellists.³⁴ In order to have a functional panel, panellists should ideally have had some knowledge of GATT. In truth, however, since governmental panellists were preferred,³⁵ panels consisted of government officials who had knowledge or had been involved in the government in the area of trade. Thus, in spite of the efforts of such panellists to act impartially, there was always the possibility that they would be influenced in their decisions by considerations of how it might affect their career and prospects in their

wheat flour from the U. S., following their dispute concerning U. S. quotas on dairy products. For details, see GATT, Netherlands Measures of Suspension of Obligations to the United States, **BISD S1/32 (1953)**; see also, *ibid.* at 62.

³⁴ See, Jackson, J. H. "Governmental disputes in International Trade Relations: A Proposal in the Context of GATT", 13 J. W. T. L. (1979) at 1.

³⁵ GATT, Decision on Dispute Settlement Procedures, **BISD S31/9 (1984)**.

countries' diplomatic service.³⁶ Third, with respect to the work by the panel, they often (especially those who were government officials dealing with the area of trade) did not make clear-cut decisions, namely, they were often reluctant to make a landmark decision which might affect not only following panel decisions but also their professional (or diplomatic) carrier back in home.³⁷

2.3.3. Delays

One of the primary complaints about the GATT dispute settlement system concerned delay, including the delays that occurred in the setting up of a panel, in the consideration of a case by a panel, and in the adoption the report of a panel by the Council.³⁸ Such delays, however, were reduced in the 1979 Understanding and also the 1982 Ministerial Declaration.³⁹ If one looks at the record over the past five years from 1987, more than a year would elapse between the Council's decision to appoint a panel and its decision to adopt the panel's report.⁴⁰

³⁶Davey, William J. , "Dispute Settlement in GATT", 11 Fordham Int'l L.J. (April 1987) at 89.

³⁷*Ibid.*, at 88-89.

³⁸The DISC case is a good example. It took almost three years to agree on the setting up a panel and further, it took another five years for the Council to adopt the panel's report. In addition, this case was the first case which outside experts were involved in a panel and it involved a kind of counterclaim to the initial complaint, which the United States insisted should be considered by the same panel as the EC complaint; see Davey, William. J., "Dispute Settlement in GATT", 11 Fordham Int'l L. J. (No. 1) Fall 1987 at 84; for the United States Tax Legislation (the DISC case), BISD S23/98 (1977); For further analysis on this case, Jackson, J. H., "The Jurisprudence of International Trade: The DISC Case in GATT", 72 Am. J. Int'l L. (1978), pp. 747-781.

³⁹The 1982 Ministerial Declaration on Dispute Settlement, BISD S29/13 to 16 (1983) [hereinafter referred to as the "1982 Declaration"], see Section 2.4.1.6. of this thesis. The 1982 Declaration stressed the need to follow the aims of the 1979 Understanding on Dispute Settlement, which stated that panels should normally be sit within thirty days of the decision to establish them and that the panel should normally report without undue delay and within three months in urgent cases.; for the 1979 Understanding, see also, *supra* note 21, para 11, 20.

⁴⁰See, *ibid.*, *supra* note 30.

2.3.4. Leakage

Some of the cps complained about the release without authorisation of the information obtained from files which had been submitted to a panel. In addition, there were some complaints concerning the early disclosure of panel reports prior to Council consideration of the matter.⁴¹

2.3.5. Consensus System

The contracting parties, including the disputing parties, were able to block the adoption of the Panel report. This was considered as a negative aspect of the previous consensus rule and the major cause of delay. Its weakness was particularly obvious, for example, in those cases concerning agricultural subsidies⁴² or foreign policy⁴³ in which the United States and the EC were involved. Since those cases involved areas of vital interest to the major economies, such countries had difficulty in accepting any solution.

⁴¹ Bael, Ivo Van, "The GATT Dispute Settlement Procedure", 22 J.W.T. No. 4 (1988) at 72; See provisions concerning protection of confidential information, paragraph 15 of the 1979 Understanding provided "...*Confidential information which is provided should not be revealed without formal authorisation from the contracting party providing the information*"; paragraph 6 (iv) of the 1979 Understanding Annex on the Customary Practice of the GATT in the Field of Dispute Settlement (Article XXIII:2) stipulating that "...*Written memoranda submitted to the panel have been considered confidential but are made available to the parties the dispute...*"; and the provisions concerning the protection of confidential information in the Tokyo Round agreements (i.e., Annex 3, para. 2 of Agreement on Technical Barriers to Trade, Article VII:9 of Agreement on Government Procurement, Annex III, para. 3 of Agreement on Implementation of Article VII, and Article 15:6 of Agreement on Implementation of Article VI).

⁴² The U. S. complaints against the EEC regarding wheat flour and pasta. In contrast, EEC complaints against the U. S. on a definition of "industry" concerning wine and grape products in the US Trade and Tariff Act of 1984.

⁴³ This type of "political" cases (i.e. a high-profile case) demonstrated a weakness or limit of GATT rules. In other words, it damaged or undermined the GATT system. Those cases were: the EC (along with Canada and Australia) embargo against Argentina during the Falklands War with the UK (30 August 1982); the US withdrawal of MFN treatment due to the treatment of democracy movement in Poland (1 November 1982); the US trade embargo against Nicaragua's policies for the Central America (5 August 1985). Recently, the WTO has received such "high-profile" complaints brought by the EC concerning the Cuban Liberty and Democratic Solidarity (LIBERTAD) Act of 1996 and other legislation enacted by the US Congress with respect to trade sanctions against Cuba. The panel has suspended its procedure at the request of the EC on 25 April 1997.

2.3.6. Fragmentation of Rules

The GATT system was complex. The co-existence of various codes caused confusion to member states.⁴⁴ The specific rules of dispute settlement procedure under the various MTN Codes in addition to the GATT general system of dispute settlement (i.e. Article XXII and XXIII), were subsumed at the Tokyo Round.⁴⁵ As a result, this multiple-choice of rules has brought an issue of "rule-shopping" or "forum-shopping" which allowed countries to a dispute to choose whichever rule was more favourable to them.

2.4. Evolution of GATT Dispute Settlement Mechanism

As mentioned, there were a number of defects in the GATT dispute settlement system. To overcome or eliminate those weaknesses or problems, the dispute settlement system has evolved via rules adopted in various meetings and rounds of negotiations, which will be examined next to demonstrate the evolutionary history of the GATT dispute settlement system.

2.4.1. Chronological Overview of Documents Relating to GATT Dispute Settlement Procedure

2.4.1.1. 1955 Report on Organisational and Functional Questions (BISD 3S/231) (Proposal Relating to Various Articles and Legal Questions)

This Report was based on proposals prepared by the Governments of Denmark, Norway and Sweden to add interpretative comments to paragraph 2 of Article XXIII of GATT. The main point concerned procedural matters, namely, that the dispute settlement rules had to be clarified to enable them to be used effectively.

⁴⁴ See, Jackson, J. H., "The Birth of the GATT-MTN System: A Constitutional Appraisal", 12:21 *Law & Policy in Int'l Business* (1980), at p. 42; Jackson, J. H., *supra* note 8, pp. 55-57.

⁴⁵ For these rules, see Jackson, J.H., *The World Trading System*, The MIT Press, Cambridge, Massachusetts, 1992, pp. 97-98.

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These countries emphasised that action by the CONTRACTING PARTIES under Article XXIII should be directed towards the maintenance of a general level of reciprocal and mutually advantageous concessions not less favourable to trade than provided for originally; in other words, it demanded that resort to retaliatory action should only arise when all other possibilities had been examined.⁴⁶

Among other proposals, the Danish delegation brought the idea of the appointment of qualified "panels" to assist in considering complaints under Article XXIII.⁴⁷ The term "panel" appeared in the GATT dispute settlement for the first time. However, at this meeting, the above idea was not discussed further. Instead, the CPs agreed to give the Executive Secretary time to consider the issue.

Nonetheless, the Danish proposal should be taken as an important turning point as well as providing a distinct contribution in term of the evolutionary history of the GATT dispute settlement system because, as will be explained later, the emergence of a panel (instead of a Working Party) marked a significant shift as regards the judicial nature of the system. In other words, unlike the Working Party, the panel system introduced impartiality by excluding the parties to a dispute from the dispute settlement process.

2.4.1.2. 1958 Procedures under ARTICLE XXII on Questions Affecting the Interests of a Number of Contracting Parties (BISD 7S/24)

This document dealt with the request of the Contracting Parties which sought the widening of the degree of participation in consultations under Article XXII of GATT. In fact, this tendency was initiated in the discussions with respect to the application of the General Agreement to the EC. The procedures adopted were as follows:

"-any contracting party seeking a bilateral consultation under Article XXII shall notify to the Executive Secretary;

⁴⁶ See, BISD 3S/250, para. 62.

⁴⁷ BISD 3S/247 (1955), para. 52; also see, as regards the history of a panel procedure, *supra* note 7.

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- any other contracting party asserting a substantial trade interest in the matter should notify its desire to join the bilateral consultation to the consulting countries and the Executive Secretary;
- if the requested party agreed that a substantial trade interest existed, the contracting party who desired to join the bilateral consultations should be entitled to participate in;
- the applicant was free to refer its claim to the CONTRACTING PARTIES if the request was not accepted;
- the consulting countries should notify the outcome of consultation to the Executive Secretary; and,
- the Executive Secretary should provide such assistance (the adopted procedures defined the involvement of the Executive Secretary) in the consultation if the parties so requested."⁴⁸

To sum up, this document was important in that it opened up access to third parties (who were indirectly affected) in order to protect their interests. In this respect, the contribution of this document was to mark the introduction of "multilateralism" under the GATT.

2.4.1.3. 1966 Report on Trade and Development (BISD 14S/139)

During the 60's, one of the major events in terms of GATT membership was the emergence of the developing countries. As a consequence, a committee was established to deal with issues relating to the amendment of the General Agreement to meet the special trade and development needs of less-developed countries which was not completed by the former Committee on Legal and Institutional Framework. The Ad Hoc Working Group on Legal Amendments, established by the Committee in 1965 to deal with these matters, had submitted an interim report.⁴⁹ The Committee

⁴⁸ Procedures under Article XXII on Questioning Affecting the Interests of Number of Contracting Parties, reprinted in BISD S7/24 (1959).

⁴⁹ See, COM.TD/F/4.

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discussed further the various proposals in the light of the findings of the Group and it reported to Contracting Parties on the following two subjects:

- a) amendment of Article XXIII to take into account difficulties experienced by less-developed countries in using that Article, and
- b) amendment of Article XVIII to authorise the use of surcharges by less-developed countries for balance-of-payment reasons⁵⁰

A proposal introduced by the Brazilian and Uruguayan delegations in 1965 for amending Article XXIII initiated the work so as to benefit the developing countries.⁵¹

Their proposal contained four elements:

"(i) the present arrangement for action under paragraph 2 of Article XXIII should be elaborated in a way which would give less-developed countries invoking the Article the option of employing certain additional measures;

(ii) where it had been established that measures complained of have adversely affected the trade and economic prospects of less-developed countries and it had not been possible to eliminate the measure or obtain adequate commercial remedy, compensation in the form of an indemnity of a financial character would be in order;

(iii) in cases where the import capacity of a less-developed country had been impaired by the maintenance of measures by a developed country contrary to the provisions of the General Agreement, the less-developed country concerned should be automatically released from its obligations under the General Agreement towards the developed country complained of, pending examination of the matter in GATT; and

(iv) in the event that a recommendation by the CONTRACTING PARTIES to a developed country was not carried out within a given time-limit, the CONTRACTING PARTIES should consider what collective action they

⁵⁰ See, **BISD 14S/139**, para. 40.

⁵¹ Dam, Kenneth W., The GATT Law and International Economic Organisation, The University of Chicago Press, Chicago, 1970 at pp. 368-373.

could take to obtain compliance with their recommendation".⁵²

The intention behind the proposal was to streamline and to set out the procedures clearly so as to speed up action under Article XXIII and go some way towards redressing the unequal bargaining position of less-developed countries vis-à-vis developed countries in proceedings under Article XXIII.⁵³

On the basis of the discussions in the Ad Hoc Group, the Committee had drawn up a revised draft decision which embodied the agreement reached in the Committee on procedures for more speedy and efficient use of the provisions Article XXIII by less-developed contracting parties, and this revised text was contained in Annex I to the report.⁵⁴

Since the fundamental concerns of less-developed countries had not been met, Brazilian and Uruguayan delegations, in particular, stated that, while they would accept the compromise reached on points (iv) as reflected in paragraph 10 of the draft decision, they could agree to a proposed draft decision only on the understanding that further work would be done with a view to resolving the two issues mentioned above as (ii) and (iii). The developed contracting parties had no objection to these issues being given further consideration in the Ad Hoc Group, but were unable to accept the proposed texts in question for various reasons which had been stated in the report of the Ad Hoc Group.⁵⁵

In agreeing that the annexed draft decision should be presented to the CONTRACTING PARTIES for adoption, the Committee also agreed that further work with regard to the two outstanding issues dealt with in the text of the two paragraphs reproduced in Annex II of the present report should be continued in the Ad Hoc Group on Legal Amendments.⁵⁶

⁵² *Ibid.*, *supra* note 50, para. 41.

⁵³ *Ibid.*, para. 43.

⁵⁴ *Ibid.*, para. 44; the Decision was adopted by the CONTRACTING PARTIES on April 5, 1966, and appears on page [D3/1].

⁵⁵ *Ibid.*, para. 45.

The Committee agreed that the phrase "shall consider what measures" in paragraph 10 of the draft decision was intended to mean that the CONTRACTING PARTIES should consider the matter with a view to finding appropriate solutions.⁵⁷

2.4.1.4. 1966 Decision on Procedures under ARTICLE XXIII (BISD 14S/18)⁵⁸

These two articles, Article XXII (Consultation) and Article XXIII (Nullification and Impairment) of GATT, played an essential role in the dispute settlement mechanism of GATT. In addition to these two articles underpinning the dispute settlement system of GATT, there was the benefit of GATT practice and of decisions taken by the CONTRACTING PARTIES. One of the examples was the adoption of the 1966 Decision on Procedures under Article XXIII (hereinafter, the "1966 Decision"), which contributed special dispute settlement procedures between developing and

⁵⁶ *Ibid.*, para. 46.

⁵⁷ *Ibid.*, para. 47.; the Chairman of the Committee on Trade and Development, in presenting the draft decision to the CONTRACTING PARTIES for adoption, asked to be placed on record the following understanding regarding its provisions:

(1) If consultations to be carried out by the Director-General under paragraph 3 of the draft decision, the Director General would, in addition to the entities mentioned in that paragraph, be free to consult such experts as he considered would assist him in studying the facts and in finding solutions.

(2) With respect to paragraph 6 of the draft decision, the CONTRACTING PARTIES may provide more particular terms of reference for any such panel in order to assist them to assess the relative impact of the measures complained of on the economics of the contracting parties concerned and to consider the adequacy of any measures which those contracting parties would be prepared to take to remedy the situation. In establishing such particular terms and reference, the CONTRACTING PARTIES or the Council should bear in mind the desirability of having such panels appraise, in particular, the following elements:

(a) the damage incurred through the incidence of the measures complained of upon the export earnings and economic effort of the less-developed contracting party;

(b) the compensatory or remedial measures which the contracting party whose measures are complained of would be prepared to take to make good damage inflicted by their application;

(c) the effects of such measures as the injured contracting party would be prepared to take in relation to the contracting party whose measures have nullified or impaired the benefits deriving from the General Agreement which the former contracting party is entitled to expect.

⁵⁸ BISD 14S/18, "Procedures under Article XXIII", Decision of 5 April 1966.

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developed countries. In addition, this document extensively dealt with a dispute involving a developed country and developing country (a new member) so that the dispute settlement system would be open and easily accessible for those new member countries. In fact, this special procedure included the Brazilian and Uruguayan plans above mentioned with the exception of some radical proposals. The main goal of these new rules were to achieve a prompt settlement of disputes filed under Article XXIII by the less-developed contracting parties.

The essential innovations introduced by the new rules, which only applied to complaints filed by less-developed contracting countries against developed contracting parties were:

- (i) the formal introduction of the DG (the utilisation of DG's good offices acting as an *ex officio* capacity) into the consultation procedures;⁵⁹

⁵⁹If consultations between a less-developed cp and a developed cp with regard to any matter falling under para. 1 of Article XXIII did not lead to a satisfactory settlement, the less-developed cp complaining of the measure might refer the matter which was the subject of consultations to the DG so that, acting in an *ex officio* capacity, he may use his good offices with a view to facilitating a solution (see, BISD 14S/18 at para.1). To this effect the cp concerned shall, at the request of the DG, promptly furnish all relevant information (*Ibid.*, para.2). The DG had to consult with the contracting parties concerned and with such other cps or inter-governmental organisations as he considered appropriate with a view to promoting a mutually acceptable solution (*Ibid.*, para.3). After a period of two months from the commencement of the consultations (para. 3 of the 1966 Decision), if no mutually satisfactory solution was reached, the DG had to, at the request of one of the cps concerned, bring the matter to the attention of the CPs or the Council, to whom he had to submit a report on the action taken by him, together with all background information (*Ibid.*, para. 4). The CPs or the Council had to immediately appoint a panel of experts to examine the matter with a view to recommending appropriate solutions. The members of the panel had to act in a personal capacity and had to be appointed in consultation with, and with the approval of, the cps concerned (*Ibid.*, para. 5). The panel had to, within a period of sixty days from the date when the matter was referred to it, submit its findings and recommendations to the CPs or the Council, for consideration and decision. Where the matter was referred to the Council, it might, in accordance with Rule 8 of the Intersessional Procedures adopted by the CPs at their thirteenth session (BISD 7S/7), address its recommendations directly to the interested cps and concurrently report to the CPs (*Ibid.*, para. 7). Within a period of ninety days from the date of the decision of the CPs or the Council, the cp to which a recommendation was directed had to report to the CPs or the Council on the action taken by it according to the decision (*Ibid.*, para. 8). If on examination of this report it was found that a cp to which a recommendation had been directed had not complied in full with the relevant recommendation of the CPs or the Council, and that any benefit accruing directly or indirectly under the General Agreement continued in consequence to be nullified or impaired, and that the circumstances were serious enough to justify such action, the CPs might authorise the affected cp or parties to suspend, in regard to the cp causing the damage, application of any concession or any other obligation under the General Agreement whose suspension was considered warranted, taking account of the circumstances (*Ibid.*, para. 9).

(ii) strict deadlines (to be fulfilled by the GATT organs in considering complaints filed by less developed contracting parties and requests for authorisation to retaliate) at some stage in the dispute settlement process.

In short, the main contribution of this decision was "velocity" which was brought about by the defining of a specific period of time in the dispute settlement procedures in respect of a case between a developed country and a developing country .

2.4.1.5. Understanding Regarding Notification, Consultation, Dispute Settlement and Surveillance (BISD 26S/210)

This document was very influential and unique in the evolutionary development of the GATT dispute settlement system, since it consisted of a detailed description of dispute settlement processes along with its Annex entitled "Agreed Description of the Customary Practice of the GATT in Dispute Settlement" (Article XXIII:2 of GATT).⁶⁰ In other words, it formed a kind of "constitutional framework", for the first time, for the GATT dispute settlement procedure. There was some initiative taken, during the Tokyo Round (1973-79), to develop the dispute settlement procedure. This task was carried out by the body called the "Group Framework Committee". This development plan, however, did not achieve much partly because of the EC's objection to any changes in the existing procedures.

The result of the negotiations became a document entitled "Understanding Regarding Notification, Consultation, Dispute Settlement and Surveillance (hereinafter, the "1979 Understanding")," which was adopted by the CONTRACTING PARTIES at their 35th Session in Geneva, 23-25 November 1979.⁶¹ Nonetheless, like the other "understandings" resulting from the Tokyo Round, the precise legal status of this

In the event that a recommendation to a developed country by the CPs is not applied within the time-limit prescribed in paragraph 8 of the 1966 Decision, the CPs had to consider what measures, further to those undertaken under paragraph 9, were to be taken to resolve the matter (*Ibid.*, para. 10). (emphases added)

⁶⁰Hudec, R. E., "GATT Dispute Settlement after the Tokyo Round: an Unfinished Business", 13 *Cornell Int'l L. J.* (1980), pp. 145-203.

⁶¹See, the 1979 Understanding in **BISD 26S/210 (1980)**, *supra* note 21.

understanding was unclear. In fact, unlike the Tokyo Round codes and other agreements, it was not a stand-alone treaty, nor a waiver under Article XXV of GATT. It was, however, presumably adopted under the general power of Article XXV to "facilitate the operation and further the objectives"⁶² of GATT.

The most noteworthy features of the 1979 Understanding were: the explicit provision for a conciliatory role for the DG; the provisions for panels; the reinforcement of the *prima facie* nullification or impairment concepts; the outline of the work of a panel including oral and written advocacy; language that permitted the use of non-governmental persons for the panels (while stating a preference for government persons); recognition of the practice of a panel report with statement of facts and rationale; and the understanding that the report was then submitted to the CONTRACTING PARTIES for a final approval.

The title of the 1979 Understanding contained the following essential elements in the GATT dispute settlement process:

- "a) a knowledge, through notifications by governments, of measures that might in the event of lead to disputes;
- b) recourse to bilateral and multilateral consultations in order, as a first priority, to reach an amicable settlement;
- c) settlement of disputes, not as a result of a quasi-judicial decision, but through recommendations conducive to re-establishment of a balance of concessions and advantage between the parties to the dispute; and,
- d) confirmation of monitoring by the Contracting Parties, thus at the same time underlining the importance of collective moral pressure in dispute settlement".

A. Notification (paras. 2-3)

With respect to notifications referred to in the 1979 Understanding, it was clear that the effective supervision of the operation of a multilateral trade treaty i.e. GATT

⁶² See, GATT Article XXV, para. 1.

required transparency in the trade regulation and measures adopted by the contracting parties. A note, dealing with the notifications which member countries were required to submit, was set up by the GATT Secretariat.⁶³ According to the 1979 Understanding, contracting parties undertook, to the maximum extent possible, to notify the CONTRACTING PARTIES of their adoption of trade measures affecting the operation of the General Agreement. It was necessary to improve notifications and the exchange of information. For this reason, the 1979 Understanding provided that, if a member country had a reason to believe that trade measures conducted by another member country were liable to upset the balance of advantage under the General Agreement, it might seek further information regarding measures at issue directly from the contracting parties concerned. Information of this kind could also be made available by the Secretariat, following a Council decision adopted after the Ministerial session in November 1982⁶⁴, which we shall see in the following section.

B. Consultation (paras. 4-6)

Consultation played a main role in the dispute settlement procedure of GATT (which it still does under the new dispute settlement system of WTO). The General Agreement provided as follows: "*each contracting party shall accord sympathetic consideration to, and shall afford adequate opportunity for consultations regarding, such representations as shall be made to it by another contracting party ...*" (Article XXII:1). If no result was arrived at through consultation, either party might request the CONTRACTING PARTIES to search for an alternative solution, usually through the establishment of a working party (later, a panel)⁶⁵ (Article XXII:2). Furthermore, if no solution was found in this multilateral consultation procedure, a contracting party might refer the matter to the CONTRACTING PARTIES under the dispute settlement procedure set out in Article XXIII:2.

⁶³ MTN/FR/W/17, 1 August 1978.

⁶⁴ The 1982 Ministerial Declaration adopted on 29 November 1982, *supra* note 39.

⁶⁵ For the Working Party and Panel, see at Sections 1.1.3.2. and 1.1.3.3. respectively in Chapter 1 of the thesis.

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Before recourse to Article XXIII:2, a preliminary phase of consultation was available either in Article XXII, or Article XXIII:1⁶⁶, or Article XXXVII:2⁶⁷. Unlike Article XXIII:1 it required written representations or one's proposals to the other contracting party or parties, and sympathetic consideration to the representations or proposals made to it had to be given under Article XXII:1. If no positive result was reached, the matter could be referred to the CONTRACTING PARTIES under Article XXIII:2. The importance of the role played by consultation could be far greater than played by procedural rules and practices. As a matter of fact, far more disputes were settled through bilateral consultation between the contracting parties in question than were dealt with by the CONTRACTING PARTIES pursuant to Article XXIII:2.⁶⁸ Accordingly, there was often no necessity to refer the matter in contention to the Council.

C. Settlement of Disputes (paras. 7-23)

GATT practice was mentioned in paragraph 5 of the Annex to the 1979 Understanding as follows: "*contracting parties have had recourse to Article XXIII only when in their view a benefit accruing to them under the General Agreement was being nullified or impaired*". If there is an infringement of obligation, normally a presumption, that a breach of the rules (under the General Agreement) had an adverse effect on other contracting parties, in such cases, it was up to the contracting parties against whom the complaint had been brought to rebut the charge. Whereas, "*if a contracting party bringing an Article XXIII case claims that measures which do not conflict with the provisions of the General Agreement have nullified or impaired benefits accruing to it under the General Agreement, it would be called upon to provide a detailed justification*"⁶⁹ (i.e. non-violation claim). This means that the

⁶⁶ BISD 9S/19.

⁶⁷ BISD 14S/20.

⁶⁸ Long, Olivier., Law and Limitation, Martinus Nijhoff Publishers, the Netherlands, 1987, at 75.

⁶⁹ Para. 5, Annex to the 1979 Understanding, *supra* note 21.

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burden of proof was on the complainant if the claim made was based on non-violation of the rules.

According to Article XXIII, a breach of the rules did not, in itself, give sufficient grounds for a dispute where there had been no nullification or impairment of a benefit under GATT. There was, however, a presumption that the incidence of a breach of the rules was unfavourable to other member countries. It was sufficient for a contracting party bringing a complaint to demonstrate that there was such a breach, and that a benefit accruing to it under the GATT was nullified and impaired, for such complaint to be considered. Nonetheless, in fact, once under way, the procedure was more concerned with a breach of the rules than with 'injury'.

The main objective of the dispute settlement was to develop an understanding between the parties in conflict, and ultimately to reach a mutually acceptable solution. The main goal was not to impose a penalty for being in breach of the GATT rules but to secure the withdrawal of the measures at issue immediately.⁷⁰ The issue of compensation only arose if the immediate withdrawal of the measures was impracticable.

Article XXIII:2 provided a contracting party with the possibility of a final course of action, namely, the suspension of the application of concession which in fact meant retaliation.⁷¹ This however needed authorisation from the CONTRACTING PARTIES.

Regarding a complaint set by a developing country against a developed country, the complainants could seek the good office of the DG.⁷² The DG might, in considering the case, consult with the Chairman of the CONTRACTING PARTIES and

⁷⁰ Cf. In this regards, the same rank of remedies can be found in the DSU, see Article 3: (i) withdrawal of inconsistent measures; (ii) compensation; (iii) retaliation.

⁷¹ See, for Netherlands Measures of Suspension of Obligations to the United States, BISD 1S/32 (1953).

⁷² See, *supra* note 59; see also Section 2.4.1.4. of this chapter.

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Chairman of the Council. Since the Ministerial Declaration of November 1982, the good offices of the DG became available to any party in dispute subject to an agreement of the other party.⁷³

According to Article XXIII:2, "*the CONTRACTING PARTIES shall promptly investigate any matter ... referred to them*". In practice, this task was entrusted to working parties or panels of experts.

The function of panels was to assist the CONTRACTING PARTIES in examining matters brought before them under Article XXIII:2. The creation of the panel was indeed the most original feature as well as the most useful element of the GATT dispute settlement procedure. (para. 16)

In the event that there was a bilateral (or mutually satisfactory) settlement between the parties to the dispute, the panel simply reported that a solution has been reached between them (normally a brief description of the case and a report that a solution had been arrived at). No further information was given. Nonetheless, a contracting party with an interest had a right to make enquiries, as far as trade matters were concerned, and to be given information about the resolution of the matter. In fact, as mentioned earlier, mutually acceptable solutions were the most popular pattern of settlement of disputes. (para. 19)

If no bilateral settlement had been reached, the panel submitted its findings and recommendations to the Council in written form, which usually included findings, observations on the applicability of relevant provisions of the General Agreement, and the main reasons for the findings and recommendations that had been made. (para. 17)

⁷³ *Ibid.*, the 1982 Ministerial Declaration, *supra* note 39.

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As soon as a panel report was adopted by the Council, rulings and recommendations set out in the report were thereby given legal force pursuant to Article XXIII:2, which provided for the CONTRACTING PARTIES "to make appropriate recommendations to the contracting parties which considered to be concerned, or give a ruling on the matter, as appropriate". In fact, no panel report or report of working party was ever turned down by the Council.

The CONTRACTING PARTIES had to maintain under surveillance any matter on which they had made recommendations or given rulings and also had to carry out a regular and systematic review of developments taken in accordance with its recommendations. (para. 22)

In case recommendations were not complied with within a reasonable period of time, further legal action provided for in Article XXIII:2 could be taken. Retaliatory measures against the party in question might be authorised. If such measures were taken that party had the option of withdrawing from the General Agreement sixty days after notifying an intention to do so.

D. Surveillance (para. 24)

The CONTRACTING PARTIES were to keep under surveillance any matter on which they had made recommendations or given rulings. If their recommendations were not implemented within a reasonable period of time, the contracting party bringing the case might ask them to intervene to find an appropriate solution. Such a request could result in a resumption of consultations and negotiations, in which case if the country's complaint were found to be justified, it would end up in a strengthened position.

The continuing surveillance by the CONTRACTING PARTIES relied for its effectiveness upon moral and political pressure. Its main goal was to secure the withdrawal of the measures concerned if they were found to be inconsistent with rules contained in the General Agreement.

To sum up, the 1979 Understanding marked a significant improvement in the dispute settlement system of GATT. As shown above, the Understanding, for the first time, accumulated and codified a large number of customary practices of dispute settlement procedures (including a special rule for a panel involving a developing country), and contributed to remove ambiguity from the dispute settlement rules. In addition, the evolution of the dispute settlement system towards "judicialisation" became even more obvious.

2.4.1.6. 1982 Ministerial Declaration on Dispute Settlement (BISD 29S/13)

In spite of the great achievements of the 1979 Understanding, there was considerable dissatisfaction with the dispute settlement procedure in GATT. A new attempt to improve the situation was made at the 1982 Ministerial meeting which was held in November 1982 in Geneva. To alleviate such dissatisfaction, the 1982 Ministerial Declaration established guidelines and commitments covering seventeen issues⁷⁴ and also reaffirmed the 1979 Understanding. As already explained, the 1979 Understanding provided the vital framework underpinning the dispute settlement procedures among contracting parties, and accordingly no major procedural amendment was required in the 1982 Ministerial meeting. Nonetheless, there was a scope for more effective use of the existing mechanism and for specific procedural improvements.⁷⁵ The dispute settlement mechanism was still being undermined by some among the contracting parties, therefore in 1982 Ministerial meeting, it was agreed that "obstruction in the process of dispute settlement shall be avoided".⁷⁶ In the end, the 1982 Ministerial Declaration made a commitment to agree on several issues to be worked upon in order to expedite the dispute settlement process. Such provisions were:

"a. Strengthening and broadening the opportunity for conciliation;

⁷⁴ See, the 1982 Ministerial Declaration, *supra* note 39, pp. 13-14.

⁷⁵ *Ibid.*, at 16.

⁷⁶ See, GATT, GATT Activities 1984 (1985), p. 16.

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- b. Enforcing compliance with established time-limits by both the panels and the CONTRACTING PARTIES;
- c. Reinforcing the CONTRACTING PARTIES' commitment to make experts available to participate on panels, and providing assistance to panels from the Secretariat;⁷⁷
- d. Encouraging clarity and responsiveness of panel decisions;
- e. Requiring panels to recommend specific causes of action and insuring that panels are responsive to the issues in their reports;
- f. Tailoring recommendations and rulings of the CONTRACTING PARTIES to achieving satisfactory settlements, ensuring follow-up of actions, and involving the parties to a dispute in the formulation of recommendations and rulings by the CONTRACTING PARTIES; and
- g. Attempting to dissuade parties from taking advantage of the consensus requirement to obstruct the dispute settlement process".⁷⁸

As stated, the 1982 Ministerial Declaration considered the issue of consensus of the CONTRACTING PARTIES in the dispute settlement system which needed to be improved in contentious areas such as consultations; the panel process; and, enforcement of panel reports and recommendations. Moreover, an innovative concept was proposed by the U.S., i.e. a "consensus-minus two" principle which aimed at avoiding blockage by the parties to the dispute at the stage of adoption of a panel report. Nonetheless, a large number of member governments rejected this proposal.

The 1982 Ministerial meeting, in general, had not achieved much progress in terms of dispute settlement procedures.

⁷⁷ See, the 1982 Ministerial Declaration, *supra* note 39, pp. 13-16.

⁷⁸ Minutes of Meeting held on 26 January 1983, C/M/165 (Feb. 14, 1983), at 3-4.



2.4.1.7. 1984 Action on Dispute Settlement (BISD31S/9)⁷⁹

The 1982 Ministerial Declaration reaffirmed that the Dispute Settlement of the 1979 Understanding had provided the necessary framework of procedures for the settlement of disputes among contracting parties.

For achieving improvements in the whole dispute settlement system, it was necessary not only to make specific procedural improvements, but also to obtain a clear-cut understanding and commitment from CONTRACTING PARTIES (or Signatories to the Codes) concerning aspects both of the nature and time-frame in: (a) the panel process; (b) the decision on the matter in dispute to be taken by the CONTRACTING PARTIES (or the Code Committee) on the basis of the panel's report; and (c) the follow-up to be given to that decision by the parties.

A number of procedural deficiencies in the panel process were encountered which could be approached within the existing framework. Such problems were, for instance, the punctual formation of panels, and the timely completion of panel reports. In spite of the guidelines for those procedures (thirty days for the formation of a panel and three to nine months to complete the panel proceedings) as stipulated in paragraph 11 and footnote 11 respectively of the 1979 Understandings, these targets were rarely met. Improvements in those aspect would not solve the shortcomings of the mechanism in their entirety. The CONTRACTING PARTIES, therefore, agreed that the following approach should be adopted to that end, on a trial basis, for a period of one year in order to continue the process of improving operation of the system. The approach taken on a trial basis could be summarised as follows:

- (i) The CPs compiled a short roster of non-governmental experts qualified to serve as panellists;⁸⁰ and

⁷⁹From the text Action taken on 30 November 1984 on Dispute Settlement Procedures (L/5752) in BISD 31S/9 (1985).

⁸⁰Formation of Panels: "Contracting parties should indicate to the Director-General that the names of the persons they think qualified to serve as panellists, who are not presently affiliated with national administrations but who have a high degree of knowledge of international trade and experience of the GATT. These names should be used to develop a short roster of non-governmental panellists to be agreed upon the CONTRACTING PARTIES in consultation with the Director-General. The roster should be as representative as possible of contracting parties". (para. 1)

(ii) In the event that the disputing parties could not agree on members of panellists within thirty days after the panel was requested, either party could ask the DG to appoint persons from the roster.⁸¹

Thus, the 1984 Action introduced a procedure, on a trial basis for one year, in order to reduce delay and to further raise the level of expertise of panellists.⁸²

2.4.2. "Trade Policies for a Better Future : The Leutwiler Report, the GATT and the Uruguay Round (1985)"

The Leutwiler Report was published in March 1985. The then DG, Arthur Dunkel, initiated the formation of an independent study group consisting of seven experts with wide experience in various fields, for instance, banking, economics, industry, and law and politics.⁸³ The main task given to this study group was to identify the fundamental factors disturbing the international trading system, and to consider a solution for the 80's. The group undertook research on problems existing in the international trading system, and finally presented fifteen recommendations in Chapter three of the Report for specific and immediate action to satisfy the crisis in the world trade order.

⁸¹ Under the same title: "In the event that panel composition cannot be agreed within thirty days after a matter is referred by the CONTRACTING PARTIES, the Director-General shall, at the request of either party and in consultation with the Chairman of the Council, completed the panel by appointing persons from the roster of non-governmental panellists to resolve the deadlock, after consulting both parties". (para. 3)

⁸² Completion of Panel Work: "Panels should continue to set their own working procedures and, where possible, panels should provide the parties to the dispute at the outset with a proposed calendar for the panel's work". (para. 1); "Where written submissions are requested from the parties, panels should set precise deadlines, and the parties to a dispute should respect those deadlines". (para. 2)

⁸³ The members of the independent study group were: Dr. Fritz Leutwiler (Chairman) (Chairman of Swiss National Bank and President of Bank for International Settlements), B. Senator Bill Bradley (US Senator, member Senate Finance Committee), Dr. Pehr Gyllenhammar (Chairman of AB Volvo), Dr. Guy Ladreit de Lacharrière (Vice President of International Court of Justice), Dr. I.G. Patel (Director of London School of Economics and former Governor of Reserve Bank of India), Professor Mario Henrique Simonsen (Getulio Vargas Foundation and former Minister of Finance of Brazil), and Dr. Sumitro Djojohadikusumo (former Minister of Trade and Industry and Minister of Finance of Indonesia).

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Regarding dispute settlement, the Leutwiler Report identified procedural problems as an area of weakness in the mechanism. Other weaknesses were also recognised in the disputes settlement process. The Report stated that "sometimes panels have had to base their findings on rules that have been superseded by tacit or informal understandings (which could be described as "ambiguity" or "art" of GATT rules)."⁸⁴ Accordingly, the following improvements to the dispute settlement procedure were recommended in the Report:

- "- panels should be set up and should complete their work more expeditiously than in some past instances;
- panels should always clearly indicate the rationale for their findings to provide the GATT Council with a firm foundation for making its decision;
- panels should be composed of experts fully familiar with the GATT legal system; such panels could be filled from a small permanent roster of non-governmental experts; such a list would facilitate the selection of panellists; frequent service by the same experts would lead to an accumulation of expertise and experience which eventually would ensure the development of consistency in the making awards building up a "case law";
- insuring enforcement of GATT obligations by allowing third party complaints when actions, such as bilateral agreements, impede the objectives of the GATT but cause no direct trade injury;
- the GATT should grant the DG power to initiate mediation and conciliation at an early stage of dispute; and
- greater and more systematic implementation of panel reports i.e. fixing dates for the carrying out of recommendations with subsequent reviews by the Council".⁸⁵

To sum up, the report may be considered to be one of the essential documents in the study of the evolution of the dispute settlement system of GATT because it put

⁸⁴ *Ibid.*, at 54.

⁸⁵ *Ibid.*, at 55-56.

forward a number of detailed proposals, some of which have subsequently become negotiating issues in the UR negotiations. Although the report was unofficial, it expressed straightforward opinions which required for preparing the ground for the forthcoming new round.

2.5. Development of Dispute Settlement Mechanism through the Uruguay Round

2.5.1. Perspectives of the GATT Dispute Settlement System - Proposal for Improvement of GATT Dispute Settlement Procedure

The principal goal of improving the GATT dispute settlement system was to ensure overall compliance with GATT rules. The Negotiating Group on Dispute Settlement (hereinafter, the "NG13") at the UR, dealing with the dispute settlement aspects of GATT, had suggested a number of matters requiring to be improved, and these were as follows:

- the encouragement of complaints by third parties concerning "grey area measures"⁸⁶;
- enhancement of the consultation process (for a settlement at an early stage, making more efforts for a settlement bilaterally before reaching a panel stage);
- increased mediation role for the DG;
- possibility to resort to binding arbitration on factual matters, provided the interests of third parties were safeguarded;
- increased use of non-governmental experts as panellists (for enhancement of the quality of legal elements of a panel and its report);

⁸⁶E.g., "Voluntary Restraint Agreements" (VRAs), "Voluntary Export Restrictions" (VER), "Orderly Market Arrangements" (OMA), etc.; see Jackson, J.H. and W. Davey, Int'l Econ. Relations, 2nd ed., West Publishing Company, St. Paul, Minnesota, 1991, pp. 609-622; see also Section 2.4.1.6. in this Chapter of the thesis.

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- acceleration of the establishment of panels and imposition of time-limits on their work (for avoiding delays);
- increased use of standard terms of reference and increased standardisation of the working procedures for panels (for avoiding delays);
- definition of specific criteria for qualifying as an interested third party, allowed to make representations to a panel;
- tighter rules on confidentiality (for termination of leakage);
- codification in a single instrument of the various texts currently governing the dispute settlement process, as amended through negotiations (for avoiding "fragmentation" of dispute settlement rules);
- requirement that parties objecting to panel rulings state their reasons in a written submission to the CP (for a prevention of easy-blockage in adopting a panel decision);
- continuing surveillance of compliance which adopted panel recommendations, for example, by scheduling regular dispute settlement meetings of the GATT Council (for encouraging an implementation of panels' ruling or recommendation, and in the event of not being implemented, maintaining supervisory political pressure on the party to whom the panel's decision to be applied until its implementation).

Several of the above suggestions were already referred to in the Leutwiler Report. Although the suggestions were adopted by the GATT system, the other proposals were excluded as part of the ongoing debate on the GATT dispute settlement system. The proposals excluded would involve a major overhaul of some of the underlying principles on which the GATT was based. For instance, a reform that had been proposed was to recognise the direct effect of GATT into national law in order to encourage private party enforcement. Another point was that the panels should be turned into permanent tribunals consisting of GATT experts. In addition, it had also

been suggested that all panel reports should be adopted by the Council and therefore, automatically become GATT law with immediate effect, or that at least the two parties to the dispute should be excluded from the consensus procedure.⁸⁷

2.5.2. 1989 Dispute Settlement Procedures Improvements: Decision Adopted at the Mid-Term Review of the Uruguay Round (April 1989) (BISD 36S/61)

Following the proposal made in the Leutwiler Report, the Ministerial Declaration on 20 September 1986 launching the UR⁸⁸ referred to negotiating goals with respect to dispute settlement mechanism: strengthening the rules and procedures of the dispute settlement mechanism; and, inventing effective measures to improve surveillance so as to achieve better compliance.

The NG 13 had already made a substantial progress in refining and improving the dispute settlement mechanism, which defined implementation on a trial basis to operate to the end of the UR.⁸⁹ In December 1988, the Trade Negotiations Committee convened in Montreal for the Mid-term Review of the UR negotiations.⁹⁰

At the April 1989 Mid-term Meeting where the trade Ministers gathered at the Ministerial level, they adopted the text agreed upon during the December 1988 meeting; it was decided that the procedural reforms would be implemented on a trial basis commencing from 1 May, 1989 until the end of the Round.⁹¹ They also agreed

⁸⁷ What was known as the "consensus-minus-two" system which was proposed by the United States at the 1982 Ministerial Resolution, which however had not been adopted in the end; for further explanation on "consensus-minus-two", see Hudec, Robert. E., The Enforcing Trade Law, *supra* note 3, pp. 232-245.

⁸⁸ Ministerial Declaration on the Uruguay Round, MIN(86)/6 (Sept. 20 1986).

⁸⁹ The CONTRACTING PARTIES later reconsidered this decision (regarding the application of the GATT dispute settlement rules and procedures on a trial basis) (BISD36S/61 on 12 April 1989) and decided as follows: "to keep the ... improvements [the 1989 Decision] in effect until the entry into force the Understanding on Rules and Procedures Governing the Settlement of Dispute contained Annex 2 of the Agreement Establishing the World Trade Organisation (MTN/FA,II); for the decision, see Decision of 22 February 1994 on Extension of the April 1989 Decision on Improvements to the GATT Dispute Settlement Rules and Procedures (L/7416).

⁹⁰ See, Trade Negotiations Committee Meeting at Ministerial Level, Montreal, December 1988, MTN. TNC/7(MIN) (Dec. 9, 1988) [hereinafter, the "1988 Mid-term Review"] at 26.

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that the NG13 should continue its work in order to achieve the negotiating objective of the Ministerial Declaration.⁹²

The Contracting Parties adopted the Mid-term Agreement concerning dispute settlement during its forty-fifth session.⁹³ They further decided that the implementation of the reforms would remain under review, a decision on their formal adoption to be made at the end of the Round.⁹⁴ Moreover, the NG13 agreed that it would continue negotiations with the aim of further improving and strengthening the GATT dispute settlement system taking into account the experience obtained in applying these improvements.⁹⁵

The 1989 Improvements played a significant role as the basis for the new dispute settlement rules which as a result became the Understanding on Rules and Procedures Governing the Settlement of Disputes (hereinafter, the "DSU").

The general provisions of the improvements to the GATT dispute settlement mechanisms which were adopted by the NG13, stated that the dispute settlement system of GATT was "*a central element in providing security and predictability to the multilateral trading system.*"⁹⁶ It further stated that "*all solutions to matters formally raised under the GATT dispute settlement system under Article XXII, XXIII and arbitration awards shall be consistent with the General Agreement...; ...the improvements set out in this document, which aim to ensure prompt and effective resolution of disputes to the benefit of all contracting parties, shall be applied on a trial basis from 1 May 1989 to the end of the Uruguay Round ...*".⁹⁷

⁹¹ See, Mid-term Meeting, MTN. TNC/11 (April 21, 1989) [hereinafter the "April 1989 Mid-term Meeting"] at 24.

⁹² *Ibid.*

⁹³ See, **Improvements to the GATT Dispute Settlement Rules and Procedures** [hereinafter, the "1989 Improvements"], Decision of 12 April 1989, L/6489, reprinted in **BISD 36S/61 (1990)**.

⁹⁴ *Ibid.*, at 62:

⁹⁵ *Ibid.*

⁹⁶ *Ibid.*

⁹⁷ *Ibid.*

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The DSU (which covers almost all issues presented in the text of the 1989 Improvements), will be analysed in Chapter 5. The following simply spells out the differences between the rules of the 1989 Improvements and the rules of the DSU of the WTO. The 1989 Improvements set out improvements in nine matters concerning the GATT dispute settlement rules and procedures: A. General Provisions; B. Notification; C. Consultations; D. Good Offices, Conciliation, Mediation; E. Arbitration; F. Panel and Working Party Procedures; G. Adoption of Panel Reports; H. Technical Assistance; I. Surveillance of Implementation of Recommendations and Rulings [cf. those items can be found in the provisions of the DSU respectively: A. (DSU 3); B. (DSU 3.6; 25.3); C. (DSU 3); D. (DSU 5); E. (DSU 25); F. (DSU 12); G. (DSU 16); H. (DSU 27; 17.7); I. (DSU 21)].

Major differences between the 1989 Improvements and the DSU are:

1. The time period for consideration of reports.

The period was 30 days in the 1989 Improvements (para. 1 of Section G), but is 20 days in the DSU (DSU 16.1).

2. The rule concerning the adoption of panel reports.

For adoption of panel reports, the practice of "consensus" was to be continued in the 1989 Improvements (para. 3 of Section G), whereas the DSU provides for an automatic adoption (through negative consensus rules) (DSU 16.4).

3. The time frame of the dispute settlement proceedings (there is a slight difference in the method of measuring the period the dispute settlement process is to take, in particular, its starting point).

The 1989 Improvements (the period from the request for Consultation until the Council takes a decision on the panel report) stated "shall not, ... , exceed fifteen months" (para. 4 of Section G).

Whereas, the DSU (the period from the date of establishment of the panel by the DSB until the date of the DSB considers the panel or appellate report for adoption)

stipulates that "shall as a general rule not exceed nine months where the panel is not appealed or 12 months where the report is appealed" (DSU 20). In advance of those time periods, the DSU stipulates that the party to which the request is made must enter into consultation "... within a period of no more than 30 days after the date of receipt of the request, ..." (DSU 4.3); that if the consultations fail to settle a dispute, "... within 60 days after the date of receipt of the request for consultations, ..." (DSU 4.7).

The provisional dispute settlement rules (on a trial base) ensured promptness and effectiveness by virtue of the 1989 Improvements. Although some matters were left out of discussion for the Brussels meeting in December 1990, the 1989 Improvements has indeed contributed to shaping the provisional rules into the draft version which later became the final dispute settlement rules (DSU).

2.5.3. The Brussels Ministerial Meeting: Draft Final Act Embodying the Result of the Uruguay Round of Multilateral Trade Negotiations (December 1990)

The Brussels Ministerial Meeting was held during 3-7 December 1990. At this meeting, the massive consolidated documentation was released. Those documents were, "Draft Final Act Embodying the Result of the Uruguay Round of Multilateral Trade Negotiations" (hereinafter, the "Brussels Draft Final Act")⁹⁸; and, the revised edition of the Brussels Draft Final Act including minor revisions as "corrigendum".⁹⁹

The Brussels Draft Final Act was a first approximation of the Final Act Embodying the Result of the Uruguay Round of Multilateral Trade Negotiations (the final version) which was finally signed on 15 April 1994 at Marrakesh, Morocco. Accordingly, the Brussels Draft Final Act included a draft of "Understanding on the Interpretation and Application of Article XXII and XXIII of the General Agreement

⁹⁸Draft Final Act Embodying the Result of the Uruguay Round of Multilateral Trade Negotiations, MTN.TNC/W/35 (26 November 1990).

⁹⁹MTN.TNC/W/35/Rev. 1 (3 December 1990).

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on Tariffs and Trade" (hereinafter, the "Draft Understanding")¹⁰⁰, which included the Commentary¹⁰¹ which listed three main issues remaining to be resolved. These issues were:

- The procedure for Council decisions concerning: the establishment of panels;¹⁰² the adoption of panel reports;¹⁰³ the adoption of appellate reports;¹⁰⁴ and, authorisation of retaliation.¹⁰⁵
- The non-resort to unilateral measures.¹⁰⁶
- Procedures for non-violation complaints.¹⁰⁷

In addition, the Draft Understanding noted two points in its footnote at the beginning of this document and those were:

- A determination has to be made with respect to the entry into force and application of this Understanding, and to the continuation of the tentative¹⁰⁸ dispute settlement procedures as decided by the Council on 12 April 1989¹⁰⁹ until the date of its Understanding's application.
- Existing dispute settlement procedures have not been recorded where bracketed alternatives proposed by negotiating parties appear, though, there were some delegations who preferred the maintenance of these present ones.¹¹⁰

¹⁰⁰ *Ibid.*, MTN.TNC/W/35, *supra* note 98, pp. 288-305.

¹⁰¹ *Ibid.* at 288.

¹⁰² See, para. 1(a) of Section D in the 1989 Improvements, *supra* note 93. In this document, the "consensus" rule was maintained. (cf. DSU 6.1)

¹⁰³ *Ibid.*, para. 4 of Section G. (cf. DSU 16.4)

¹⁰⁴ *Ibid.*, para. 3 of Section H. (cf. DSU 17.14)

¹⁰⁵ *Ibid.*, para. 3 of Section L. (cf. DSU 22.7)

¹⁰⁶ *Ibid.*, Section M. (cf. DSU 3.1; 23)

¹⁰⁷ *Ibid.*, Section P. (cf. DSU 26)

¹⁰⁸ See, Footnote 1 in the Draft Understanding, *supra* note 98 at 289.

¹⁰⁹ See at Section 2.5.2. in Chapter 2 of the thesis; see also BISD 36S/61, *supra* note 93.

¹¹⁰ *Ibid.*, Footnote 2 in the Draft Understanding, *supra* note 98 at 289.

At the Brussels Ministerial meeting, nothing much happened regarding the issue of institutions to which dispute settlement matter belonged.¹¹¹ The two major outstanding issues listed above (i.e. the question of decision-making of the Council; and the proposed non-resort to unilateral action) were not discussed. Instead, the main focus was placed upon non-violation complaints. Accordingly, the rest of the outstanding issues were carried over to the following negotiations.

In short, despite its importance, little progress was achieved on dispute settlement mainly due to a lack of political commitment. Nonetheless, the overall structure and contents of the Draft Understanding were, in essence, almost identical to the text of the final version of the present DSU.

2.5.4. Draft Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations (MTN.TNC/W/FA) (20 December 1991)

On 20 December 1991, the then Chairman, Arthur Dunkel, released the "Draft Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations".¹¹² This Dunkel Draft stressed the need for further effort to conclude the negotiations. This section presents a brief outline of the Dunkel Draft, while its detail being more accessible in the guide of the last version entitled "The Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiation" (hereinafter, the "Final Act") as discussed in Chapter 5 of this thesis. The Dunkel Draft dealt with the issue of dispute settlement in two draft agreements: "Understanding on Rules and Procedures on Dispute Settlement"; and, "Elements of an Integrated Dispute Settlement System".

¹¹¹ Under the "Institution", there were also issues on Final Act and FOGS (Functioning of the GATT System).

¹¹² MTN.TNC/W/FA (20 December 1991) [hereinafter, the "Dunkel Draft"].

2.5.4.1. Understanding on Rules and Procedures on Dispute Settlement

(MTN.TNC/W/FA S. 1-S. 23) (20 December 1991)¹¹³

The Dunkel Draft included an exhaustive presentation of the results reached at negotiations in almost all the negotiating groups. It was further emphasised that the Dunkel Draft would not be deemed a final agreement¹¹⁴ until ongoing negotiations were completed as a whole package, which should include pending areas such as market access and trade in services. The Dunkel Draft Understanding integrated the interim procedures adopted after the Mid-term Review¹¹⁵ (functioned as a trial basis since then), the Brussels Draft Understanding,¹¹⁶ and the October 1991 revisions to the Brussels Draft.¹¹⁷ The unified text covered issues regarding procedures for Council decisions (e.g. automaticity in the establishing of panels, adopting panel reports and authorising retaliation), political commitment to refrain from unilateral action, non-violation complaints, and treatment of developing countries. Furthermore, the Dunkel Draft Understanding reiterated that existing rules of the GATT concerning dispute settlement (i.e. Article XXII and XXIII) would remain in effect until the date of entry into force of the Understanding.¹¹⁸ It further expressed that new requests under Article XXII:1 and XXIII: 1 of GATT had to be conducted according to the Understanding when it became effective. In addition, it was also agreed that a full review of GATT dispute settlement rule and procedures, had to be completed within four years of their effective date when the trade ministers would make a decision whether to continue, modify, or terminate relevant procedures¹¹⁹ at the first meeting at Ministerial level after completion of the review.

¹¹³This document was a part of the Dunkel Draft and dealt with dispute settlement rules; MTN.TNC/W/FA S.1-S.23 [hereinafter, the "Dunkel Draft Understanding"].

¹¹⁴*Ibid.*

¹¹⁵See at Section 2.5.2. in Chapter 2 of the thesis.

¹¹⁶See, *ibid.*, Section 2.5.3.

¹¹⁷*Ibid.*, at S. 1.

¹¹⁸*Ibid.*

¹¹⁹*Ibid.*, at S. 2. (cf. the current deadline is at the end of July 1999)

2.5.4.2. Elements of an Integrated Dispute Settlement System (MTN.TNC/W/FA T.1-T.6)

The Elements of an Integrated Dispute Settlement System¹²⁰ set out objectives to harmonise and conform the various procedures of dispute settlement, which were to deal with the GATT and its associated Agreements, the Tokyo Round Codes, the GATS agreements, the TRIPs agreements and the PTAs. The idea was to terminate the possibility of "forum-shopping" or "rule-shopping" which had appeared especially after the introduction of the Code signed at the Tokyo Round. The new idea of "integrated" dispute settlement system was meant to wipe out that problem as well as to eliminate the complexity of the rules of dispute settlement as a whole.

The main issues covered in this agreement were: Dispute Settlement Body; Establishment of Panels; Composition of Panels; Terms and Reference of Panels; Conflict of Substantive Provision; Compensation and Suspension of Concessions; Non-violation Complains; and, Suspension of Concessions. The analysis of this document has been left to the following chapters where the new dispute settlement system of WTO as a final product of the document are dealt with.

¹²⁰Like dispute settlement rules mentioned above as the "Dunkel Draft Understanding", (MTM.TNC/W/FA S.1-S.23), *supra* note 113, this document is also a part of the Dunkel Draft, MTN.TNC/W/FA T.1-T.6.

Chapter 3 THE NEGOTIATION HISTORY OF THE DSU

Introduction

The dispute settlement negotiations of the UR were investigated by the member states' recognition of the urgent necessity, owing to the defective GATT system, to establish an effective mechanism to resolve international trade disputes. To achieve that end, the members agreed to tighten up rules and procedures of the dispute settlement mechanism, and to enhance surveillance of implementation in order to strengthen enforcement of panel decisions. However, there were two distinctive views on the role of GATT dispute settlement. One group, led by the U.S. with some support from Canada and other countries including developing countries, regarded the role of dispute settlement system as means of arriving at a judgement in a quasi-judicial manner. The other group, supported by the EC and Japan, considered that the panel procedure of dispute settlement should be understood to be a continuation of conciliation.

The aim of this chapter is to describe the position of the major negotiating parties (i.e. EC, Japan, U.S. and the developing countries) and to highlight disagreements between those who viewed the dispute settlement mechanism as being judicial in character and those with a contrary opinion as to its characters. In order to carry out this enquiry, this chapter mainly examines the working papers of the dispute settlement mechanism submitted to the NG13 during the early period of the UR. Furthermore, in this chapter, working papers are presented and examined in chronological order. The negotiation period covered in this chapter will be limited to the period up to 1988 just before the Montreal Ministerial meeting (5-7 December 1988) because most of the key issues in the negotiations were raised and discussed extensively before this meeting. In fact, this draft was reviewed by the trade Ministers during the meeting and was formulated in a text consisting of initial rules and procedures of dispute settlement. In April 1989, the Contracting Parties adopted

the text as a tentative rule on a trial basis until the finalisation of the then ongoing UR negotiations.

3.1. Initial Proposals by Member Countries

The NG13 held its first meeting on 6 April 1987.¹ At the first meeting, participants placed emphasis on a means of securing compliance with GATT. The participants also made proposals of a preliminary nature in respect of specific issues to be considered in the forthcoming negotiations. Those issues raised were: the nature of dispute settlement; the establishment of panels; the work of panels; the role of the GATT Council; implementation of panel reports; equal access to the GATT dispute settlement system; and strengthening of the GATT dispute settlement system through the involvement of third interested parties.

U.S. Position:

Subsequent to the initial meeting, the negotiating group convened its second meeting on 25 June 1987.² The United States put forward suggestions in a discussion paper,³ and made the following points:⁴

- (1) It is necessary to enhance the mediation role of the GATT DG or his designee.⁵
- (2) The necessity to establish a binding arbitration process (involving no need for GATT Council or Code Committee approval) as an alternative means of dispute settlement for defined classes of cases, or by prior agreement of the disputing parties on an *ad hoc* basis.⁶

¹MTN.GNG/NG13/1 (10 April 1987).

²See, Meeting of 25 June 1987, Note by the Secretariat [hereinafter, the "June 1987 Meeting"], MTN.GNG/NG13/2 (15 July 1987).

³See, Improved Dispute Settlement: Elements for Consideration, Discussion Paper Prepared by United States Delegation [hereinafter, the "U.S. Discussion Paper"], MTN.GNG/NG13/W/6 (25 June 1987).

⁴See, *ibid.*

⁵Cf. *ibid.*, Article 5:6 of the DSU.

⁶Cf. *ibid.*, Article 25.

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(3) The requirement to lay down binding and enforceable timetables for the process in its various stages.⁷

(4) That non-governmental experts could be appointed as panellists, and this would be to everyone's advantage.⁸

(5) The benefits to be derived from the use of the same terms of reference by all panels as standard in order to prevent delays caused by negotiating terms which differ in accordance with those who are the parties to the dispute.⁹

(6) A procedure to deal with the problem of blocking the adoption of panel reports¹⁰; and/or

(7) As an alternative to the ideas in item (6), it was suggested that the parties should seek to implement the recommendations resulting from a settlement to a dispute, and recognise that failure to do so gives rise to a right to compensation or retaliation.¹¹

Many of the proposals of the U.S., towards judicialisation, have been adopted in the new dispute settlement rules in the DSU.

Japan's Position:

Subsequent to the U.S. proposal, Japan in its Communication at the second meeting of the NG13 noted that "*existing dispute settlement of the GATT has been functioning by and large well*".¹² Japan further stated in this communication that "*the task ...in the Uruguay Round is to materialise the collective political commitments on strengthening the dispute settlement mechanism*".¹³

According to Japan's written communication, the predominant reasons for the system being cumbersome and slow resided in the panel proceedings and included: the tendency to resort to panel procedures without sufficient bilateral consultations in

⁷Cf. *ibid.*, Article 20 and para. 12 in Appendix 3 to the DSU.

⁸Cf. *ibid.*, Article 8:1, 4; see for a short roster of non-government panellist in L/5752 in BISD 31S/9 (1985).

⁹Cf. *ibid.*, Article 7.

¹⁰Cf. *ibid.*, Article 16:4; the U.S. Discussion Paper, *supra* note 3.

¹¹Cf. *ibid.*, Article 22.

¹²See, Communication from Japan, MTN.GNG/NG13/W/7 (1 July 1987).

¹³*Ibid.*

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advance;¹⁴ insufficient relevant GATT articles and/or the lack of uniformity in interpretation of those articles.¹⁵ Japan therefore indicated what in its view the necessary improvements were:¹⁶

"(1) Clarification is necessary regarding the relationship between consultations under Article XXII and XXIII:1, or good offices of the DG and the recourse to a panel;

(2) The mechanism for using good offices of an appropriate body for conciliation (paragraph 8 of the 1979 Understanding) must be improved;

(3) Regarding the selection of panel members, review and enlargement of the indicative list of qualified persons in the roster (paragraph 13 of the 1979 Understanding), and more frequent use of non-governmental persons in the roster to be invited to serve as panellists;

(4) For the sake of speedy procedures in the setting up of a panel, procedures in the Council to decide on the setting-up a panel should be modified in order to facilitate more expeditious decisions. (For example, one of the guide lines should be to clarify the maximum period allowed to the panel proceedings, the meaning of the terms "cases of urgency" in paragraph 20 of the 1979 Understanding must be clarified, and the procedures under paragraph 16 of the 1979 Understanding, "*adequate opportunity to be given by panels to develop a mutually satisfactory solution,*" must be also clarified); and,

(5) Concerning the procedural improvements for the adoption of panel reports, for the implementation of the panel recommendation (for instance, the explicit indication of the reasonable period for the implementation of a panel recommendation, the necessary measures must be taken by the Council in case of non-compliance by the end of the said period). In extreme cases,

¹⁴Regarding this aspect, one example should be mentioned here, i.e. Japan Alcoholic Beverages Case, L/6216 (13 October 1987) in BISD 34S/83 (1988): The case was initiated by the EC's request for a consultation with Japan as provided for in GATT Article XXII:1 in 1985. After two sessions of consultations had failed, the EC requested to set up a panel as provided in GATT Article XXIII:2. Japan, however, did not agree with the establishment of the panel on the ground that *consultations had not been exhausted as defined in GATT Article XXII:1*. (emphases added); see for the reasons given by the Government of Japan in C/M/205 (12 December 1986) at 8.

¹⁵*Ibid.*; for further explanation of this matter, see Chapter 7 of this thesis.

¹⁶*Ibid.*

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compensation and retaliatory measures must be taken. The existing provision which states that the Council's (or the CONTRACTING PARTIES') authorisation is necessary prior to such actions should be retained, as it may be useful for in revisal of domestic legislation and the enforcement and implementation of GATT obligations".¹⁷

Japan further submitted a subsequent communication with suggestions for further development, in which it suggested that "*the CONTRACTING PARTIES should not accept the request of a complaining party to refer a matter to it, unless the parties concerned go through bilateral consultations under Article XXIII:1.*"¹⁸ In other words, bilateral consultations must be strengthened and the concomitant procedures should also be clarified further.

It should be noted here was another significant contribution, during the UR negotiation, made by Japan to the dispute settlement system, i.e. its insistence on the inclusion of a provision regarding prohibition of unilateralism [now in Article 23 of the DSU].¹⁹ Interestingly, in fact, this Japanese contribution is clearly reflected on its attitude towards DS in actual cases, which will be examined in Chapters 7 and 8 (case studies).

In addition to the Japanese insistence on the prohibition of unilateral actions, the proposal made by the Nordic countries also sought to tackle the same issue. In their view, the U.S. had justified its recourse to the unilateral measures under the Section 301 by criticising the limitation of the GATT jurisdiction. The disputes brought to the GATT were diverse and often referred to issues that had not been dealt with in the past and for which there were no previous experience. Thus, the dispute

¹⁷See, *ibid.*, *supra* note 13, pp. 2-3; The U.S. strongly opposed this point until the end of the round negotiations and eventually, it succeeded in maintaining its position. Instead, the U.S. agreed to compromise with another point which can be seen, as a final agreement, in Article 23 of the DSU which narrowed the possibility of unilateral actions.

¹⁸Communication from Japan [hereinafter, the "Japan Proposal September 1987"], MTN.GNG/NG13/W/9 (18 September 1987).

¹⁹Unfortunately, not much of these Japanese efforts are documented. For this reason, this information was given through the interview with an ex-government official of Japanese government in June 1998, Geneva.

settlement system needed to be improved so as to make it more flexible and efficient to cope with a diversity of new problems.²⁰

EC's Position:

The EEC(EC) proposed in its communication that the Community recognised the importance for the credibility of the GATT system of speedy and efficient settlement of disputes in order to bring benefits to all contracting parties.²¹ In addition, the Community supported the negotiating objectives, that is, to improve and strengthen the rules and procedures for the dispute settlement. The Community indicated its position in the communication as follows:

(1) Analysis of the nature and functioning of the machinery²²

The main objective of the GATT dispute settlement machinery is to reach mutually satisfactory solutions to the disputes within the context of a multilateral framework, and to restore the balance of economic and trade advantages that have been nullified or impaired. The Community was of the opinion that a satisfactory solution to disputes should be sought in conciliation, negotiation, and consensus.²³

(2) The practice of consensus²⁴

Consensus rule remained the traditional method of settling disputes as it had been adopted in November 1982 at the Ministerial Declaration.²⁵

Any new procedure providing for an automaticity in the process to adopt panel reports and to implement recommendations would bring a great change in the GATT dispute settlement system.

(3) Specific improvements to be made to the existing procedures²⁶

The Community agreed to the view that the functions of conciliation and mediation should be strengthened, and the arbitration procedure could be

²⁰See, Communication from the Nordic Countries, MTN.GNG/NG13/W/10 (18 September 1987).

²¹See, Communication from the EEC, MTN.GNG/NG13/W/12 (24 September 1987).

²²Cf. Article 5:1 of the DSU.

²³*Ibid. supra* note 21, para. 1 at 1.

²⁴*Ibid.*, para. 2 at 2.

²⁵Section (x) in L/5424, BISD 29S/13 (1983) at 16.

²⁶*Ibid.*, *supra* note 21, Section (a) and (b), para. 3 at 2.

institutionalised.²⁷

With respect to panel procedures (e.g. right to the establishment of a panel, terms of reference of panels, composition of panels, fixing of time-limits in panel procedure), however, no major proposal was made and its views on panel procedure followed the existing method in general.

(4) Adoption of panel reports and the implementation of recommendations²⁸

The Community stated that the practice of the method of consensus should remain within the Council's decision making process as mentioned above. The question, however, was how to reconcile the requirement of maintaining this practice with the other requirement of avoiding situations that weakened the credibility and effectiveness of the dispute resolution system. One answer to this could be that an improvement in the quality of the panel reports and the provision of more details as to the reasoning behind the findings. The other improvement should be that parties raising objections to a panel finding should submit a written opinion to the CONTRACTING PARTIES in order to give reasons for their action.

In addition, reasonable time-limits for implementation of recommendations adopted by the Council could be clarified.²⁹ Finally, the Community expressed that the idea of strengthening the Council's monitoring of the implementation of recommendation should be agreed upon.³⁰

The Community, in its final remarks of the communication, called for the codification of the various existing texts on dispute settlement (Article XXIII of GATT) so as to produce a single consolidated text.³¹ The intention behind this request brought by the EC was to eliminate the

²⁷Cf. Article 5:5 and Article 25 of the DSU.

²⁸*Ibid.*, *supra* note 21, Section (d), para. 3 at 4.

²⁹Cf. Article 21:3, 4 of the DSU.

³⁰See (iv) Transparency at Section 5.3. in Chapter 5 of this thesis; cf. *ibid.*, Article 21.

³¹*Ibid.*; for the list of a single "consolidated" text (including Annex 1A; B; C, Annex 2 and Annex 4), i.e. agreements covered by the DSU, see Appendix 1 to the DSU.

fragmentation of dispute settlement arrangements under GATT that had arisen due to the variety of scattered procedures established under a number of Tokyo Round codes.³²

3.2. Responses from Negotiating Countries

This section examines the responses of the negotiating countries to the suggestion made at the initial stage of negotiations, mainly with regard to the following aspects: nature of the dispute settlement system, the panel process, adoption and implementation of panel decisions, and other procedural rules.

Japan's Position:

Japan disagreed with the proposal of the establishment of a binding arbitration procedure supported by the United States, the E.C., and other negotiating countries. The reason was that this procedure "*could undermine the competence of the CONTRACTING PARTIES under Article XXIII:2 to examine and authorise counter-measures.*"³³

Japan also disagreed with the binding enforceable timetables which were proposed for the panel process. The reason for the disagreement was that it "*could result in the abuse and proliferation of counter-measures.*"³⁴

Japan further expressed some doubt concerning the idea of selecting non-governmental experts as panellists "exclusively" with more frequency.³⁵

Concerning other procedural aspects, Japan put forward the view that the danger of abusive usage of a panel by third countries may cause an indirect negative effect on the GATT system.³⁶

In addition, the Japanese delegation also disagreed with the Australian proposal that a panel might also recommend that compensation be extended to any interested third

³²*Ibid.*, *supra* note 21 at 5.

³³Meeting of 21 and 24 September 1987, Note by the Secretariat [hereinafter, the "21/24 of September 1987 Meeting"], MTN.GNG/NG13/3 (12 October 1987) at 4.

³⁴*Ibid.* at 5.

³⁵See, The Japan Proposal September 1987, *supra* note 18 at 5.

³⁶Cf. Article 4:11 and Article 10 of the DSU.

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parties, because the Australian proposal "*could cause an unwarranted spillover of bilateral disputes*".³⁷

Finally, the Japanese representative proposed the strengthening of the confidentiality of panel proceedings.³⁸

The United States was quite satisfied with the proposals submitted in the NG13 because the U.S. proposals (e.g. the shortening of the timetable for panel consideration, the stipulation of standard terms of reference, and the expansion of the role of the DG to set down terms of reference and panel composition in case the parties to the dispute were unable to reach an agreement within a limited period of time) which would clarify and expedite the existing dispute settlement process were all covered.

Furthermore, the U.S. had received support from a number of negotiating members with regard to the following matters: the expansion of the roster of non-governmental panellists; the increase of surveillance control over panel reports in the process of being implemented; and the consolidation of all GATT texts on dispute settlement procedures.

As for other proposals, the U.S. commented on the need to amend procedures in order to allow for the adoption of panel reports excluding disputing parties. On this matter, the EC made an objection to the U.S. view.³⁹ The U.S. noted that this idea was in need of further examination because there was still the possibility of panel reports being blocked by "surrogated" parties. In this regard, one could notice a clear difference in the opinions between the EC and the U.S. Namely, the EC supported the conventional consensus requirement, whereas the US was ready to exclude disputing parties from the strict consensus requirement (including those parties in dispute), which implied a U.S. preference of a judicial approach to this issue.

³⁷See, Meeting of 9 November 1987, Note by the Secretariat [hereinafter, the "9 November 1987 Meeting"], MTN. GNG/NG13/4 (18 November 1987) at 4.; the United States also expressed its accord, stating that the necessity of clarification for the third party rights, to the Japanese position.

³⁸*Ibid.*

³⁹The EC's view on this respect was expressed in its additional communication in 1988, see MTN.GNG/NG13/W/22, *infra* note 96, at 2; see also at Section 3.3. of this chapter.

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The U. S. delegation also questioned how the term "a material interest" was to be defined,⁴⁰ which related to proposals to exclude parties with "a material interest" in a dispute stemming from Council decision on panel reports.

The U.S. further concerned itself with the positions of the EC and Japan regarding blockage of a report, and wondered whether the requirement of written justification for blocking reports would be enough to prevent the granting of approval for a "bad-intent" one.⁴¹ The U.S. again expressed its preference for the judicial approach, i.e. once a panel report was ready, no party could block its adoption (i.e. automatic procedure). Meanwhile, the Australian delegation raised the issue that disputing parties and third parties with a material interest in a dispute should not participate in Council decisions on the adoption of the panel report.⁴² In this respect, the Australian position seemed to support that of the U.S.

The EC delegation replied to many questions raised regarding the inability of bilateral arbitration to reduce the competence of the CONTRACTING PARTIES to interpret the General Agreement and to protect the rights of third parties.

The developing country group proposed several points in the early negotiations. For instance, Brazil advocated special treatment for less-developed contracting parties.⁴³ Its delegation made a proposal stating that a developing contracting party must be given differential and more favourable treatment in cases of disputes arising between developing contracting parties with limited retaliatory power and a developed contracting party.⁴⁴

⁴⁰See, The 9 November 1987 Meeting, *supra* note 37 at 3.

⁴¹*Ibid.*

⁴²See, *ibid.* at 4.

⁴³Cf. Article 24 of the DSU; other provisions related to this issue can be found in Article 3.12; Article 4.10; Article 8.10; Article 12.10, 11; Article 21.2, 7 and 8.

⁴⁴See, The 21/24 of September 1987 Meeting, *supra* note 37 at 6; a special attention for those developing countries can be seen in the WTO Agreement, particularly in the DSU, after the Uruguay Round negotiation, for example, Article 3:12 (General provisions), Article 4:10 (Consultation), Article 8:10 (Composition of panel), Article 12:10, 11 (Panel procedure), Article 21:2, 7, 8 (Surveillance of Implementation of Recommendations and Rules), Article 24 (Special Procedures Involving Last-Developed Country Members), and Article 27:2 (Responsibilities of the Secretariat/ Training Courses); see also Decision of 5 April 1966 in BISD 14S/18.

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The Korean delegation supported the idea submitted by the United States, Japan, and the EEC (EC), which was to enhance the dispute settlement mechanism by means of consultations, conciliation, and mediation.⁴⁵ The idea of binding arbitration should be limited to cases where disputing parties had agreed to refer the dispute to arbitration. Korea supported the automatic panel establishment after consultations and an appropriate examination of the issues in the Council had taken place. Korea also agreed to the use of the standard terms of reference, a proposal made by the Japanese delegation. Regarding the period of the completion of a panel process, the Korean delegation proposed nine months from the establishment of the panel as an acceptable maximum, and three months in urgent cases. The delegation also noted that the Council should decide by consensus on the adoption of panel reports, within sixty days and thirty days in urgent cases, from the date of the submission of the report. Any objecting party should make written submissions explaining its position during this period.⁴⁶

The delegation of Hong Kong explained the objectives of the negotiations as follows: "*negotiations shall include the development of adequate arrangements for overseeing and monitoring the procedures that would facilitate compliance with adopted recommendations*".⁴⁷ Hong Kong supported the proposal submitted by Australia and the EEC (EC) to strengthen the surveillance function of the Council on matters arising from disputes in the GATT. Hong Kong also proposed the possibility of setting up a separate GATT body to decide on dispute settlement. This body would report to the Council and could perform its functions regarding dispute settlement. The body would meet at regular intervals to keep any existing disputes under review and also examine the functioning of the dispute settlement mechanism. Alternatively, as an alternative to such an additional new body, the Council should meet regularly in a "dispute settlement mode" and examine and monitor dispute settlement matters.⁴⁸ In addition, the chairman of the Council meetings should be

⁴⁵See, *ibid.*, *supra* note 3, 12, 18 and 21 for MTN.GNG/NG13/W 6, 7, 9, and 12.

⁴⁶See, *ibid.*

⁴⁷See, The 21/24 of September 1987 Meeting, *supra* note 33 at 6.

⁴⁸This proposal became a model of the present system, namely, the General Council of the WTO convenes as two more function: Dispute Settlement Body (DSB) as provided for in the

available for conciliation.⁴⁹

A joint communiqué submitted by the delegations of Argentina, Canada, Hong Kong, Hungary, Mexico and Uruguay expressed concern regarding the Dispute Settlement Council, particularly since the majority of GATT dispute settlement proceedings involved the participation of developed countries and this, in turn, might make the agenda of the Council meetings in a "dispute settlement mode" reflect too much the view of the developed countries.⁵⁰ The developing countries, therefore, felt isolated from the dispute settlement system and this, for them, was an unsatisfactory situation.⁵¹ Accordingly, one delegation suggested that the regular Council meetings could be extended to deal with dispute settlement instead of creating a special session for that purpose.⁵²

The other delegations noted that the establishment of a new body, the GATT Dispute Settlement Council, could dilute the competence and importance of the regular GATT Council, and worse, weaken the GATT dispute settlement process itself.⁵³ The delegations also explained that the new body would not prevent the less-developed countries from exercising their rights under the process.⁵⁴

3.3. Further Negotiation on the Dispute Settlement Mechanism

By the early 1988, it became clear to all participants in the negotiation on dispute settlement that the proposals put forward fell into two distinct categories: (1) those

DSU; and Trade Policy Review Body (TPRB) as provided for in the TPRM (Trade Policy Review Mechanism), see Article IV, para. 3 and 4 of the WTO Agreement respectively.

⁴⁹See, *ibid.*

⁵⁰See, Meeting of 20 November 1987, Note by the Secretariat [hereinafter, the "20 November 1987 Meeting"], MTN.GNG/NG13/5 (7 December 1987) at 3.

⁵¹"For a long time, the GATT was basically a club that was primarily of relevance to OECD countries. Developing countries did not participate fully." in Hoekman, Bernard. and Michel Kosteci, The Political Economy of the World Trading System - from GATT to WTO, Oxford University Press, Oxford, 1995, at 235; By contrast, under the new WTO system, developing countries have begun to use multilateral procedures for resolving disputes much more than they did in the past., for cases to prove such trend, see GATT, GATT Focus No. 112, November 1994.

⁵²*Ibid.*, *supra* note 55 at 3; No detail was given for the "delegation" in the document.

⁵³*Ibid.*; No detail was given for the "delegation" in the document.

⁵⁴*Ibid.* at 4.

for essentially procedural improvements to the existing arrangements, and (2) those which would involve fundamental change.

Japan's Position:

Japan submitted a supplementary proposal based on the 1987 discussions.⁵⁵ The purpose of this proposal was to facilitate discussions in the NG13. This proposal mainly stressed two issues: the problem of undue obstruction to the adoption of a final report, and arbitration.

With respect to the issue of adoption of a final report, Japan supported the rule of adoption by consensus because of the following two reasons: First, the practice of consensus ensured the effective implementation of the decisions of the panel by simultaneously establishing the wishes of the CONTRACTING PARTIES and that of the disputing parties. Second, the effective functioning of the GATT dispute settlement procedures in the past with respect to the implementation of the panel decisions was partly attributable to the merit of the consensus practice.

Japan, however, disagreed with the proposal of a "consensus-minus-two" which consists of excluding the parties to a dispute from the decision-making process of the panel report. In addition, the idea of "consensus-minus-two" would, in its view, create more difficulties in settling a dispute in accordance with the panel decision considering the different views held by different countries on the legal binding nature of the panel decision. Japan thought that the undue obstruction to its adoption was a result of either the flaws in a panel report or the complexity of the disputes themselves.⁵⁶ Japan considered the following two approaches were necessary to overcome the situation of "obstruction of adoption":

- (1) To improve the quality of the panels by ensuring that proper legal or factual judgements are taken; and
- (2) To endorse the Council's decision to grant a disputing party an opportunity to raise an objection to the panel report, as suggested in the Korean Proposal⁵⁷ and to review the panel report within a specified period of

⁵⁵See, Communication from Japan [hereinafter, the "Japan Proposal 1988"], MTN.GNG/NG13/W/21 (1 March 1988).

⁵⁶*Ibid.*, at 3.

time prior to the adoption of panel report in case of objection.⁵⁸

Judging from those points raised by Japan, it seems that Japan indicated its preference for dispute settlement rules with a more judicial nature (though, along with the EC, Japan was believed to be in favour of non-judicial one at the beginning) and taking into account the approaches indicated above, made a counter-proposal against suggestions made by a number of delegations as follows:

(1) Improvement of the quality of the panels

-It could be improved by appointing persons to the panels, as panellists, who have the necessary expertise in the GATT provisions, international trade, and the industries involved.

-It is also important to expand and improve the function of the Secretariat in general, for example, that the number of the Secretariat legal staff⁵⁹ should be expanded so as to facilitate the rendering of adequate technical assistance or service to panel proceedings.

(2) Procedures to raise an objection to a panel report⁶⁰

-It is necessary to avoid undue delay in the dispute settlement procedures and for this purpose, an explicit procedure to have an opportunity for raising a formal objection to the panel report should be instituted. The procedure would be as follows:

⁵⁷See, 2 (e) of the Communication from Korea, MTN.GNG/NG13/W/19 (20 November 1987) at 5.

⁵⁸See, The Japan Proposal 1988, *supra* note 55 at 4.

⁵⁹As of May 1999, there are ten legal officers excluding the Director who normally directly involved in some high-profile/big cases, in the Legal Affairs Division of the WTO Secretariat. My personal impression after my internship (April-June 1997) at the division is that the division is understaffed in general, *inter alia*, if they receive a number of big cases at the same period of time, then it would be very difficult to keep and manage those cases running within the strict time-frame designated in the DSU. Nonetheless, the possibility of increasing the staff number seems, in general, rather low due to the budgetary requirements of the WTO Secretariat. In practice, normally the director appoints two officers to be in charge of each panel as a panel secretary and/or legal officer (sometimes, one more officer as an assistant).

⁶⁰Cf. Article 16:4 of the DSU; also for appeal, *ibid.*, Article 17.

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- "-The objecting party should submit a written explanation of objections to the CONTRACTING PARTIES (i.e. the Council) specifying the compelling reasons;
- the CONTRACTING PARTIES should give sufficient consideration to reviewing the communication and could use it in deliberating the panel report; and
- the review should be completed within thirty days"⁶¹.

In the meantime, with respect to arbitration as a formal means of GATT dispute settlement procedures, Japan considered that it should be made available only if the following conditions were met: i) neutrality of an arbitral body; ii) consistency and transparency of the enforcement; and iii) discrete nature (i.e. limited applicability) of findings. The details for each of those conditions are as follows:

i) Neutrality of an Arbitral Body:⁶²

Japan thought it essential that an arbitrator be neutral in order to avoid the situation where one disputing party takes advantage of political or economic leverage to impose unfair arbitrators or awards on another party. Japan also proposed that, with a view to achieving neutrality in arbitration, an arbitral body established by the CONTRACTING PARTIES in Geneva would be ideal. Concerning the selection of arbitrators, Japan suggested that the qualifications and nomination procedures of panellists should be clearly laid out and applied in order to ensure the neutrality of arbitrators.

ii) Consistency and Transparency of the Enforcement:⁶³

Japan also made proposals promoting consistency and transparency in the arbitration proceedings. According to the opinion of Japan, the mandate of an arbitral body must be limited to fact-finding, and any interested third party

⁶¹See, Section (d) in the Japan Proposal 1988, *supra* note 55 at 6. It states that "*Such a reviewing procedure should be invoked to ensure an objective assessment of the matter and prompt settlement of the dispute with due respect for the purposes of the GATT dispute settlement procedures. It shall not be intended or considered as a device to bring about delay of the settlement of the dispute.*"

⁶²*Ibid.*, Section 2, para (1) at 7.

⁶³*Ibid.*, para. (2) at 8.

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should have an opportunity to raise objections to the arbitral awards. Moreover, any disputing party should have the right to consult with the CONTRACTING PARTIES in the event of an arbitration award adding to or diminishing the rights and obligations provided in GATT.

iii) Discrete Nature (or Limited Applicability) of Findings.⁶⁴

Japan proposed that the findings of an arbitration awards be effective only as regards the specific matter referred to in the arbitration, and that, in any case, the awards bind only the parties to the arbitration.

Japan's 1988 proposal on dispute settlement was reviewed at the NG 13 meeting in 1988.⁶⁵ With respect to the supplementary proposal of Japan, one delegation supported the opinion expressed by Japan, i.e. doubt over the "consensus-minus-two" idea, and also backed the introduction of a written submission to justify an objection to the adoption of a panel report,⁶⁶ but proposed that the review procedure be conducted in a separate forum from the contentious arguments regarding the dispute.

Furthermore, the NG 13 welcomed the idea of the introduction of a voluntarily agreed arbitration as proposed by Japan.⁶⁷ In addition, the Group also supported Japan's suggestion for the need for a degree of control by the Council over the object-matter of the arbitration.⁶⁸ It was suggested, however, that the Council's control over third party objections to an arbitration award could limit the right to a panel by making that right conditional upon a Council's *prima facie* case of nullification or impairment.⁶⁹

Another delegation proposed that a modified consensus (i.e. consensus minus the parties to a dispute and, possibly, interested third parties) could be applied without

⁶⁴*Ibid.*, para. (3) at 9.

⁶⁵See, The Meeting of 2 and 3 March 1988, Note by Secretariat [hereinafter, the "March 1988 Meeting"], MTN.GNG/NG13/6 (31 March 1988).

⁶⁶No identity for the "delegation" was given in this document.; *ibid.* Section 7 at 3.

⁶⁷Cf. *ibid.*, Article 25, para. 2 of the DSU.

⁶⁸*Ibid.*, *supra* note 70.

⁶⁹*Ibid.* at 3-4.

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weakening the effectiveness of the consensus principle.⁷⁰ In fact, this was the veto power, given to individual contracting parties based on the consensus principles, which had caused unwarranted delay on many occasions in the past, and furthermore this power had indeed weakened the credibility of the GATT system as a whole.⁷¹ Accordingly, the modified consensus could improve the existing situation with reference to the resolution of disputes. Furthermore, the modified consensus would reinforce the GATT rules to the benefit of all contracting parties and facilitate to restore balance between parties.⁷² This delegation explained that the exclusion of the disputing parties was not based on bad faith but on the knowledge that the persuasiveness of one's own arguments and the merits of one's own case row so overwhelm one's own judgement that one was frequently incapable of seeing alternative solutions.⁷³

Another delegation supported the proposals of Japan suggesting the need for expansion in the following areas: improvement of the panellists' roster, increase of secretariat resources, and submission of a written reasoning when objecting to a panel report.⁷⁴ With respect to the last point, the proposed procedure for raising objections, this delegation noted that such procedure could be a repeat of the arguments presented before a panel.⁷⁵

The delegation also expressed its concern about the proposal that one arbitral body serve for all arbitration, and further questioned whether the same individuals should serve as arbitrators in every cases.⁷⁶ What would happen if a dispute involved a national of one of the disputing parties as an arbitrator?⁷⁷ The delegation further questioned the validity of the suggested direct Council consideration of third party objections consequent to binding arbitration without referring to Article XXIII:1 which provides for objecting parties wishing to hold bilateral consultations.⁷⁸

⁷⁰No identity for the "delegation" was given in this document; *ibid.* Section 9 at 4.

⁷¹*Ibid.*

⁷²*Ibid.*

⁷³*Ibid.*

⁷⁴No identity was given for the "delegation" in the document; *ibid.*, Section 11 at 5.

⁷⁵*Ibid.*

⁷⁶*Ibid.*, at 6.

⁷⁷*Ibid.*

Japan's Position:

Commenting on the various responses to its proposals, Japan reiterated the merits of the consensus practice which contains "*the key to the proper functioning of the GATT dispute settlement mechanism and to the effective implementation of dispute settlement findings of the Council.*"⁷⁹

Japan also noted that the review of written objections to a panel report must be conducted within a limited period of time.⁸⁰ The Japanese delegation further mentioned that in order to avoid a repetition of arguments, the Council should decide which issues of a panel report should be examined.⁸¹ Regarding the proposed arbitration procedure, Japan supported the opinion that the right of the third parties to raise objections and to invoke Article XXIII should not be limited.⁸² The mandate of the Arbitration however, should be limited to fact-finding unless the CONTRACTING PARTIES had specifically authorised in advance a broader arbitration mandate beforehand.⁸³

EC's Position:

The previous communiqué of the European Community⁸⁴ referred to an analysis of the nature and functioning of the GATT dispute settlement mechanism and its views on specific improvements to be achieved in existing procedures. In 1988, the EC submitted additional views on some elements and defined its position regarding issues which arose in the 1987 negotiations.⁸⁵ This communication dealt with (1) adoption of panel reports, (2) conciliation/mediation procedures, (3) arbitration procedure, (4) deadlines concerning panel procedures, and (5) surveillance. With this proposal, the EC intended to stimulate the stagnating situation and to achieve progress in the negotiation. The details of each issue were:

⁷⁸*Ibid.*

⁷⁹*Ibid.*, Section 17 at 9.

⁸⁰*Ibid.*

⁸¹*Ibid.*

⁸²*Ibid.*

⁸³*Ibid.*

⁸⁴See, MTN/GNG/NG/13/W/12, *supra* note 21.

⁸⁵See, Communication from the EEC, MTN.GNG/NG13/W/22 (2 March 1988).

(1) Adoption of Panel Reports

First of all, the EC had not taken a definitive position on the issue of the adoption of panel reports and on the making of recommendations. Although a number of suggestions had been made, these tended to make non-adoption more difficult by requiring written reasons to justify objections to a panel report, by limiting the opportunities for rejecting a panel report by excluding the disputing parties from the adoption of a decision, or by circumventing the problem by making panel reports binding unless there was no consensus against the adoption of a panel report (what is known now as the "negative consensus" rules).⁸⁶ The EC indicated that the problem would arise because of competing views about the essential purpose of the dispute settlement process:

"...from the angle of a trade dispute, it may seem illogical that one of the parties could become, ..., both judge and jury in its own case; and ...from the angle of interpreting GATT rules, it would seem equally illogical that a Contracting Party should be excluded from the process of interpretation which belongs to the Contracting Parties as a whole."⁸⁷

The EC noted that three possibilities seem to be worthy of consideration in order attempt to reconcile these problems:

- "i) To keep the existing practice of adoption by consensus, but to make it more difficult to obstruct a consensus for adoption for political reasons. This might be resolved by providing a better structured mechanism in order to justify such oppositions (e.g. written submissions to the GATT Council or Code Committees);
- ii) the consideration of panel reports could facilitate adoption. Concerning a legal finding, the existing consensus of all Contracting Parties would be required. With respect to decisions made on the recommendations, these should be taken in a more flexible manner. (e.g. a consensus would be considered to exist even if one of the parties to the dispute has difficulties in accepting that recommendations); and,

⁸⁶*Ibid.*, Section 1 at 1-2.

⁸⁷*Ibid.*, at 2; see the U.S. view on this issue: "...the adoption of panel reports without the participation of disputing parties." at Section 3.2. in this chapter.

iii) in the event consensus was impossible to arrive at, the Council would take note of the panel report. Nonetheless, the Council would seek a decision on the recommendations in a pragmatic manner as proposed above".⁸⁸

(2) Conciliation/Mediation Procedures

In the light of past GATT practise, neither conciliation nor mediation was favoured. This situation can be explained by the fact that "*the parties concerned prefer to insist on their rights on a multilateral level instead of accepting conciliation/mediation on an ad-hoc basis*".⁸⁹ Therefore, these additional procedures, which if used by the parties in the event of their bilateral consultations failing, proved unpopular. In any event, the EC disagreed with any structured or compulsory conciliation/mediation procedure since it was likely to prolong the proceedings, although it accepted that conciliation/mediation should remain as an option.⁹⁰

(3) Arbitration Procedure

The EC proposed that an arbitration system as a supplementary technique of dispute settlement be added to the existing system. The EC stressed the following points in the light of the idea of setting up an arbitration system:

- the institutionalisation of a rapid arbitration procedure would facilitate the resolution of certain disputes, specially, those factual questions;
- arbitration as a supplementary technique would be made available dependent upon the mutual agreement of the parties involved;
- decisions of the arbitral tribunal would be binding for the parties involved in it but should not interfere with the GATT rights of third parties; and
- the GATT Council would be informed of the arbitration result and could take appropriate decisions if necessary".⁹¹

⁸⁸*Ibid.* at 3.

⁸⁹*Ibid.*, Section 2.

⁹⁰*Ibid.*

(4) Deadlines Concerning Panel Procedures

The EC argued that it is important to set deadlines for the process in order to expedite the process of the examination of disputes and also avoid delays in any of procedures which usually follow. Panels, however, should stay free to establish their own flexible timetable. The EC suggestions were:

- "- the Council should decide to establish a panel, normally at the first meeting, or at the latest, by its second meeting following the one where the request was made;⁹²
- standard terms of reference should be used, unless the disputing party, within 10 working days, agrees to alternative terms of reference;⁹³
- if there is no agreement between the parties involved within 10 working days, the DG, in consultation with the Chairman of the Council, should determine the composition of the panel;
- the standard working procedure of the panel should be determined by the panel and could be formally adopted by the CONTRACTING PARTIES, and it should not exceed nine months (3 months in case of urgency) for the presentation of the panel report to the Council;⁹⁴
- the Council must examine the report within 30 days from the date of their presentation;⁹⁵ and
- parties to whom recommendations are addressed should agree on a reasonable period, (i.e. 6 to 12 months), in order to implement recommendations".⁹⁶

(5) Surveillance

The EC also stressed the importance of having a strengthened and regular procedure of surveillance and a controlled dispute settlement procedure. The

⁹¹See, *ibid.* at 4.

⁹²Cf. Article 6:1 of the DSU.

⁹³The EC view on this point share with that of Japan and the US; cf. Article 7 of the DSU.

⁹⁴Cf. Article 12: 8 of the DSU.

⁹⁵Cf. Article 16: 4 of the DSU.

⁹⁶Communication from the EEC, MTN.GNG/NG13/W/22, *supra* note 85, Section 4 at 4-5; cf. Article 21:3 of the DSU.

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EC, however, noted that the Council's surveillance only covers dispute matters arising from Article XXIII, thereby excluding dispute matters brought under the MTN Codes, i.e. the Tokyo Round Codes, where competence for surveillance should be limited to the Signatories' Committees.⁹⁷ The EC stated that, instead of establishing a new *ad hoc* mechanism, the Council should continue functioning as it does now.⁹⁸

At a meeting in March 1988, one delegation commented on the EC's proposal and found that the EC's submission did not mention the situation where disputing parties blocked the adoption of panel reports even though the panel had reached a consensus.⁹⁹ This delegation expressed its interest in the EC proposal on adoption of reports, i.e. "*the consideration of the general conclusions as regards GATT conformity separately from the specific recommendations for remedy.*"¹⁰⁰

With respect to arbitration, the delegation felt that arbitration would not redress the existing differences over the adoption and the implementation of panel reports.¹⁰¹ The delegation, more generally, supported the proposed deadlines to be applied to the panel process.¹⁰²

Another delegation expressed their agreement with the proposed optional conciliation and mediation, the submission of written objections to explain reasons, and also with the proposed deadline.¹⁰³ In addition, the delegation also supported an enhanced surveillance procedure which contained positive elements in it (e.g. helps in identifying a violator of rules as well as facilitates the implementation of a ruling made by a Panel (or Appellate Body)).¹⁰⁴ On the other hand, the delegation regarded

⁹⁷See, *ibid.* at 5.

⁹⁸*Ibid.*

⁹⁹See, The March 1988 Meeting, *supra* note 64 at 5; no identity for the "delegation" was given in this document; this EC's stance for the issue could be explained by the fact that the EC was one of most popular contracting parties along with the U.S. which often had blocked the adoption of final reports.

¹⁰⁰*Ibid.*

¹⁰¹*Ibid.*

¹⁰²*Ibid.*

¹⁰³No identity for the "delegation" was given in this document; see, *ibid.* at 6.

¹⁰⁴*Ibid.*; cf. Art. 21.6; 22.8 of the DSU.

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the blocking of the adoption of panel reports as one of the serious matters to be tackled in the dispute settlement mechanism.¹⁰⁵

Regarding the establishment of a panel, the delegation thought that one Council meeting should be sufficient to decide on a panel establishment.¹⁰⁶ The delegation, furthermore, questioned the necessity of limiting arbitration to fact-finding and noted that objecting third parties should retain their rights under Article XXIII.¹⁰⁷

¹⁰⁵ *Ibid.*

¹⁰⁶ *Ibid.*

¹⁰⁷ *Ibid.*

Chapter 4. THE SYSTEM OF WORLD TRADE ORGANISATION **(WTO)**

Introduction

The WTO¹ was set up on 1 January 1995 as a result of the UR negotiations which were concluded on 15 December 1993.² The Ministers of member governments supported its results by signing the Final Act at the Marrakesh Meeting of April 1994 in Morocco. In the Marrakesh Declaration of 15 April 1994, the Ministers affirmed that the conclusion of the UR negotiation would "*strengthen the world trade economy and lead to more trade, investment, employment and income growth throughout the world*".³ The Marrakesh Agreement Establishing the World Trade Organisation (hereinafter, the "WTO Agreement"), therefore, the successor to the General Agreement, could be described as the embodiment of the ideas discussed at the UR. In fact, the agreement makes provisions as regards the principal contractual obligations that determine how the governments of the members frame and implement domestic trade legislation and regulations. Moreover, the WTO has now become the "forum" where trade relations among countries evolve through collective debate, negotiation, and adjudication.

This chapter provides a brief description of the institutional and constitutional structure of the WTO and further demonstrates the evolutionary (i.e. judicial) character of the new system in comparison with the previous GATT system. An investigation of its dispute settlement mechanism which will be conducted in the next chapter.

¹For an overview of the World Trade Organisation in general, see McGovern, Edmond., International Trade Regulation, Globefield Press, Exeter, 1995; Stewart, Terence P. (ed.), The World Trade Organisation, American Bar Association, Section of Int'l Law Practice, Washington D.C., 1996; Qureshi, Asif H., The World Trade Organisation, Manchester University Press, Manchester, 1996.

²Final Act Embodying the Result of the Uruguay Round of Multilateral Trade Negotiations, MTN/FA (15 December 1993) [hereinafter, the "Final Act"].

³For the Marrakesh Declaration of 15 April 1994 in the GATT Secretariat, The Results of the Uruguay Round of Multilateral Trade Negotiations: The Legal Texts, Geneva, June 1994.

4.1. Objectives of the WTO⁴

The World Trade Organisation is an international organisation. In the Preamble to the WTO Agreement, the drafters basically reiterated the objectives of the old GATT: the primary purposes are: the substantial reduction of tariffs and other barriers to trade and the elimination of discriminatory treatment in international trade relations; while the supplementary purposes are: the raising of standards of living and incomes, sustainable development and the preservation of the environment, the ensuring of full employment, expanding production and trade, and the optimal use of the world's resources, while at the same time extending these aspirations to services.

Over and above these considerations, the underlying objective of the WTO is to create a comprehensive framework of rules capable of governing the world trading system in its widest sense, including, as stated in the WTO Agreement, the objective of making provisions to enable the conditions which are necessary for a "sustainable development". The idea of a "sustainable development" in relation to "*the optimal use of the World's resources*"⁵, comes hand in hand with the need to protect and preserve the environment in a manner consistent with the various levels of national economic development.

Elaborating on the ideals of the institution, the WTO Agreement recognises that "*there is need for positive efforts designed to ensure that developing countries, and especially the least developed among them, secure a share in the growth in international trade with needs of their economic development.*"⁶ Accordingly, the WTO Agreement stresses once again the necessity of special support for the

⁴For the text of Marrakesh Agreement Establishing the World Trade Organisation, [hereinafter, the "WTO Agreement"], *ibid*; and for the table of the Agreement's structure, see Appendix I to this thesis.

⁵Although the Preamble to the WTO Agreement is mainly based on that of the GATT, there is a slight difference between them, i.e., "*the optimal use of the world's resources*" of the former has been altered from "*full use of the resources of the world*" of the latter. (emphases added) The term "optimal" being used in the former Preamble seems to have more flexible and wider definition than the term "full" as used previously in the latter. Thus, it seems that perhaps the WTO intended to enlarge the meaning of this phrase in order to prepare for its future or potential issues.

⁶See, the Preamble to the WTO Agreement.

developing countries in order that the multilateral trade system can come into full effect both fairly and effectively.

To contribute to the achievement of these objectives, the Members of WTO have agreed to enter into "*reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade and to the elimination of discriminatory treatment in international trade relations*"⁷ and moreover determined "*to develop an integrated more viable and durable multilateral trading system.*"⁸

As showed above, the aim of WTO is based on that of GATT but moreover it emphasises the multilateral trading system along with a wider scope and fairer and more effective elements.

4.2. Legal Structure of the WTO Agreement⁹

It seems rather daunting to comprehend the structure of the WTO Agreement since it is so wide reaching and comprises voluminous texts. To ease such obstacles, this section offers a guide to the WTO Agreement.

To begin with, the WTO Agreement consists of two major parts: (1) the WTO Charter which defines the institutional measures of the WTO; and, (2) the Annex which contains four Annexes prescribing substantive rules. As each one of them has different objectives it may therefore have different legal consequences in its respective area of influence.

⁷ *Ibid.*

⁸ *Ibid.*

⁹ For the structure of the WTO Agreement, see Appendix 1 to this thesis; for a general summary of the background and the system of the WTO, see, Evans, Phillip and James Walsh, The EIU Guide to the New GATT, The Economist Intelligence Unit, London, 1994; Hoekman, Bernard., and Michel Kostecki, The Political Economy of the World Trading System: From GATT to WTO [hereinafter, referred to as the "Political Economy"], Oxford University Press, Oxford, 1995, Chapter 2, pp. 36-55; for a discussion on the WTO system, see, Jackson, J.H., "The World Trade Organisation, Dispute Settlement, and Codes of Conduct", in Collins, Susan M., and Barry P. Bosworth (eds.), The New GATT: Implications for the United States (Brookings Occasional Papers), The Brookings Institution, Washington D.C., 1994 at pp. 63-75;

First, the WTO Charter is laid out in sixteen articles that furnish the definitions of the fundamental aspects of the WTO under the title of "a single institutional framework". Although the most important structural aspects of the institution will be dealt with in other sections of this chapter, the present section will focus on the four principle Annexes, i.e., Annex 1, 2, 3, and 4.¹⁰

(1) **Annex 1:** Annex 1 is subdivided into three Annexes, namely, Annex 1A, 1B, and 1C. Annex 1 deals with the "multilateral agreements", all of which are of the "mandatory" kind. All WTO member states have, therefore, entered into a number of binding obligations that result from those agreements, and which are:

-Annex 1A: This Annex includes the General Agreement on Tariffs and Trade 1994 (hereinafter, the "GATT 1994") consisting of six understandings and the Marrakesh Protocol to the General Agreement on Tariffs and Trade 1994 (hereinafter, the "Protocol to the GATT 1994") which in turn contains twelve agreements;

-Annex 1B: This Annex deals with the General Agreement on Trade in Services (hereinafter, the "GATS") which was not included under the GATT 1947 and also covers the schedules dealing with tariff concessions; and,

-Annex 1C: This Annex concerns the Agreement on Trade-Related Aspects of Intellectual Property Rights (hereinafter, the "TRIPs") which was not referred to in the GATT 1947.

(2) **Annex 2:** The Annex 2 exclusively defines the dispute settlement rules. It is entitled "Understanding on Rules and Procedures Governing the Settlement of Disputes" (hereinafter, the "DSU"). These rules are mandatory for all WTO members. More importantly, this dispute settlement system could be called an "integrated" one because it allows all of the WTO members to base their claims or complaints on any of the multilateral trade agreement clauses incorporated in the Annexes to the WTO Agreement. As Annex 2 deals with the main issue of my

¹⁰ See, in general, Appendix I to this thesis.

dissertation, i.e., the rules of dispute settlement, this topic will be analysed exhaustively in the next chapter. As we will see next, however, the procedures set out in Annex 3 (TPRM) were excluded from this dispute settlement mechanism.

(3) **Annex 3:** This Annex describes the Trade Policy Review Mechanism (hereinafter, the "TPRM") which enables the WTO to review regularly and to make reports on the trade policies and practices of the WTO Member states as a matter of course.¹¹ The mechanism, however, is not intended to become a legal basis, either for enforcement of the obligations under the WTO Agreement or for the dispute settlement procedure.¹² The main concern of the Trade Policy Review Body (hereinafter, the "TPRB"), the organs in charge of TPRM, is to examine the impact of the trade policies and practices of the member states on the multilateral trading system as a whole, and to produce reports about their findings. Nevertheless, we may safely assume that the TPRM could function as a sort of "stopper" for the WTO Members in order to avoid generating trade disputes among them. In fact, so far, it is operating well as regards fulfilling that expectation. Because Members are requested to submit a regular report describing their trade policy, which can be regarded as a "disclosure" of strategy or policy, there is less possibility for a trade dispute to break out among them.¹³

¹¹ See Annex 3, C (Procedures for review) of the WTO Agreement; each Member of WTO is requested to submit periodic reports, explaining its trade policies, and whose frequency of reviews depends on a function of a Member's share of world trade. In other words, the burden of issuing a report is determined based on the economic size of each member state. For example, the four largest world economies, known as the "Quad", (i.e. the U. S., the E. U, Japan, and Canada) are be required to undergo a review by the WTO General Council every two years. The next sixteen economies will be reviewed every four years. The rest of WTO Members will be reviewed every six years. Nonetheless, there is an exception for least-developed country Members to which a longer period may be applied, and this could be regarded as a special consideration for those countries to achieve a balanced trading relationship under the philosophy of true "multilateralism".

¹² As Hoekman noted, "...the TPRM suffers from important limitations - e.g. reports are not analytical enough to provide an evaluation of the economic effects of various national policies and cannot serve as a basis for dispute settlement..." in Hoekman, B., The Political Economy, *supra* note 9 at 45, whose comments are from Curzon-Price, V., "GATT's New Trade Policy Review Mechanism", 14 *World Economy* (1991), pp. 227-38, and also from Mavroidis, Petros C., "Surveillance Schemes: The GATT's New Trade Policy Review Mechanism", 13 *Mich. J. Int'l L.* (1992), pp. 374-414.

(4) **Annex 4:** Originally, this Annex included four "plurilateral agreements", though only two of them currently remain,¹⁴ which are "optional". In other words, the agreements are binding only on those countries who have signed one of those agreements.

One concern is the non-compulsory nature of those agreements which seems contrary to the main concept of a "single-undertaking" (i.e. all the round agreements applying to all GATT contracting parties) underlying the WTO Agreement. Nevertheless, this non-compulsory nature provided this Annex with much room for further possibilities. In other words, the WTO is able to continue the development of its areas of concern or of new subjects, as the WTO evolves and tries to keep pace with the fast-changing world of trade. In addition, the WTO has readied itself for the incorporation of new member states, and the changes newcomers might create for a new trade environment in the future.

To sum up, the WTO Agreement is not only more detailed but also anticipates future development of world trade, which should help in avoiding a major amendments to the present system. These precautions must have been taken because of experience of GATT. In short, unlike the old GATT, the WTO Agreement contains a certain flexibility based on stringent and firm legal foundations.

4.3. Scope of the WTO¹⁵

Let us now turn to the scope of the WTO which is stipulated in Article II of the WTO Agreement.

¹³ Professor Petersmann described this notion as "preventive policy" and "conflict avoidance strategy", which support the WTO rules for the mandatory settlement of disputes, see Petersmann, E.-U., The GATT/WTO Dispute Settlement System, Kluwer Law International Ltd., London, 1997 at 57.

¹⁴ Among the original four plurilateral agreements, International Dairy Agreement and International Bovine Meat Agreement were terminated from the Annex 4 of the WTO Agreement at the end of 1997; see Press/78 (30 September 1997), Deletion of the International Dairy Agreement from the Annex 4, Decision of 10 December 1997, WT/L/251 (17 December 1997), Deletion of the International Bovine Meat Agreement from Annex 4, Decision of 10 December 1997, WT/L/252 (16 December 1997).

¹⁵ See Article II, the WTO Agreement.

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First of all, the WTO provides the common institutional framework for the conduct of trade relations between its Members in matters concerning the agreements and associated legal instruments as it appears in the Annexes to this Agreement (para. 1);

There are agreements and relevant legal documents in Annex 1, 2 and 3, i.e., the Multilateral Trade Agreements (hereinafter, the "MTAs") which are integral parts of this Agreement and which are binding on all Members (para. 2);

In addition, as already mentioned, the agreements and associated legal documents of Annex 4, i.e., the Plurilateral Trade Agreements (hereinafter, the "PTAs") are also part of this Agreement, though, only for those members that have accepted the PTAs. The PTAs are, therefore, "stand-alone agreements", in other words, and their binding capacity concerns only those members who have signed one of those agreements (para. 3); and,

Finally, the GATT 1994 is legally separate from the General Agreement on Tariffs and Trade signed on 30 October 1947 (hereinafter, the "GATT 1947"), which was annexed to the Final Act Adopted at the Conclusion of the Second Session of the Preparatory Committee of the United Nations Conference on Trade and Employment, as subsequently rectified, amended or modified (para. 4).

4.4. Functions of the WTO¹⁶

The WTO performs five functions which are set out in Article III of the WTO Agreement and those are:

1) Administering and implementing the multilateral and plurilateral trade agreements which together make up the WTO:

The WTO facilitates the implementation, administration and operation, and promotion of the objectives of the WTO Agreement and the MTAs. Furthermore, it provides the framework for the implementation, administration and operation of the PTAs.

¹⁶ See Article III, the WTO Agreement.

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2) Playing the role of forum for multilateral trade negotiations:

The second paragraph of Article III states that the WTO will make available a forum for negotiations between its Members concerning matters of multilateral trade relations. This is achieved under the agreements set out in the Annexes to the WTO Agreement. In addition, the WTO makes available to its members a forum for further negotiations within the framework of the multilateral trade negotiations as well as a framework for the implementation of the results of such negotiations. Decisions concerning implementation may be made by the Ministerial Conference which will be held at least once every two years.

3) Seeking to resolve trade disputes:

The third paragraph in Article III states that the WTO administers the DSU as stipulated in Annex 2 to this Agreement. Since it is one of the most important functions of WTO and furthermore the main topic of the thesis, this particular function will be analysed extensively in the next chapter.

4) Overseeing national trade policies:

The fourth paragraph of Article III states that the WTO also administers the TPRM as stipulated in Annex 3 to this Agreement. Although there was a long-established practice of trade policy review during the GATT period, the separate agreement relating to TPRM was annexed to the WTO Agreement. The decision to establish a TPRM was made on 12 April 1989 in "Functioning of the GATT System (FOGS)".¹⁷

¹⁷ See L/6490, BISD 36S/403, section D at 405.

5) Co-operating with other international institutions involved in global economic policy-making:

The last paragraph in Article III states that the WTO co-operates with the International Monetary Fund (IMF) and with the International Bank for Reconstruction and Development (hereinafter, the "IBRD") and its affiliated agencies in order to achieve greater coherence in global economic policy-making.¹⁸ Whereas, pursuant to the purpose of the Bretton Woods system which had been created after World War II, the GATT provided for, in Article XV, co-operation with the IMF. The GATT had already practised co-operation with the IMF and the World Bank and therefore there was a GATT precedent in this regard.

4.5. Institutional Structure of the WTO¹⁹

The arrangements concerning the institutional structure of the WTO are provided for in Article IV of the WTO Agreement, as follows:

(1) The highest organ of WTO is the *Ministerial Conference*,²⁰ which is composed of representatives of all the Members and is convened, at least, once every two years. The Conference accomplishes the functions of the WTO and takes the necessary actions to this effect. The Conference has the authority on the request of a Member state to take decisions on all matters under any of the MTAs subject to and in accordance with the specific requirements for decision making set out in this Agreement and in the relevant MTA (para. 1).

¹⁸ *Ibid.*

¹⁹ See the WTO Agreement, Article IV; for a diagram of the WTO institutional structure, see, WTO, WTO Focus, No. 1 (January-February 1995) at 5.

²⁰ The first WTO Ministerial Conference was held in Singapore between 9-13 December 1996. The second WTO Ministerial meeting was held in Geneva between 18-20 May 1998, which was combined with a celebration of the 50th anniversary of the multilateral trading system. The third one is scheduled in Seattle, U.S., for 30 November - 3 December 1999.

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(2) In addition, all the Member states send representatives to a *General Council*. The Council takes the place of the Ministerial Conference in the intervals between its meetings and it is assigned the functions carried out by the Conference when it is in session. The Council sets up its rules of procedure and approves rules for the Committees as set out in paragraph 7 (para. 2);

the General Council meets to discharge the responsibilities of the DSB as is required by the DSU (Annex 2); the DSB has its own chairman and makes provisions for the setting out of the rules of procedure necessary for the fulfilment of those responsibilities (para. 3);

the General Council also convenes to discharge the responsibilities of the TPRB as laid out in the TPRM (Annex 3); the TPRB has its own chairman and sets out the rules of procedure for the fulfilment of those responsibilities (para. 4).

(3) The complexity of the institutional structure seems to stem from the numbers of organs which perform a variety of duties. Among them, for example, there is a *Council for Trade in Goods*, a *Council for Trade in Services*, and a *Council for Trade-Related Aspects of Intellectual Property Rights* (hereinafter, the "Council for TRIPs"), which perform their respective functions under the general guidance of the General Council (para. 5); the Council for Trade in Goods supervises the functioning of the MTAs provided for in Annex 1A; the Council for Trade in Services supervises the functioning of the GATS; the Council for TRIPs supervises the functioning of the TRIPs; these Councils perform the functions allocated to them by their respective agreements and also by the General Council; subject to the approval of the General Council, these Council establish their own rules of procedure; representatives of all Member are able to have memberships in these Councils; these Councils convene when it is necessary to perform their functions (para. 5); each of these Councils sets up subsidiary bodies on their request; such subsidiary bodies provide for their respective rules of procedures subject to the approval of their respective Councils (para. 6).

(4) The Ministerial Conference establishes a *Committee on Trade and Environment*, a *Committee on Trade and Development*, a *Committee on Balance-of-Payments Restrictions*, and a *Committee on Budget, Finance and Administration*, which perform functions allotted to them by the WTO Agreement and by the MTAs, and any additional functions allocated to them by the General Council, and may establish such additional Committees with such functions as may be deemed appropriate; as part of its functions, the Committee on Trade and Development occasionally reviews the special provisions in the MTAs to assist the least-developed country Members and reports to the General Council for appropriate action; any representatives of any members are able to be members of these Committees (para. 7).

(5) The bodies provided for under the PTAs, i.e., a *Committee on Civil Aircraft*, a *Committee on Government Procurement*, (an *International Dairy Council*, an *International Meat Council*),²¹ carry out the functions allocated to them under those Agreements and operate within the institutional framework of the WTO; these bodies keep the General Council informed of their activities (para. 8).

(6) The structure of the *Secretariat* is stipulated in Article VI. The head of the Secretariat is the Director General (DG), as defined in Article VI (1), who is appointed by the member countries at the Ministerial Conference. The staff members of the Secretariat are appointed by the DG and are exclusively independent and international in character, and in charge of all the secretarial works of WTO under the supervision of the DG. While, the responsibility of the Secretariat concerning dispute settlement is specially stipulated for in Article 27 of the DSU. In addition, there are a number of provisions providing for the further functions of the Secretariat.²²

²¹ See, *supra* note 14.

²² See, for example, DSU 8.1; 8.4; 8.6, 12.6 and Decision on Certain Dispute Settlement GATS 5.

4.6. How Different is the WTO from GATT?²³

The World Trade Organisation is not a mere extension of GATT. WTO, as an institution, has indeed replaced GATT and, in the process, has acquired quite a different character. The most important differences are:

(1) The WTO is an international institution in its own right:

The WTO is a permanent institution with its own Secretariat.²⁴ Conversely, GATT was originally initiated as a multilateral agreement and which could be described as a set of rules albeit that GATT was arguably recognised as a *de facto* international organisation.²⁵ In fact, the GATT had no institutional foundation, although there was a small associated *ad hoc* Secretariat²⁶ whose origins can be traced to the failed attempt in the 1940's to establish an organisation expected to become the International Trade Organisation.

The commitments of the WTO are full and permanent, whereas the GATT was applied only on a "provisional" basis even though the member countries, termed "Contracting Parties" treated it almost as a permanent organisation.²⁷

(2) The trade area covered by WTO is considerably wider than that of the old GATT:

Apart from the coverage of trade in goods as it was in GATT, the WTO covers new sectors of trade such as Trade in Services, Trade-Related Aspects of Intellectual

²³ See in general, WTO Focus, No. 1, *supra* note 19 at 4.

²⁴ The WTO Agreement sets out a provision concerning "the Secretariat" in Article VI and "Status of the Secretariat" in Article VIII, whereas no provision was provided in the General Agreement (i.e. the GATT 1947) as such.

²⁵ See, in general, Henry G. Schermers, International Institutional Law, 3rd ed., Sijthoff & Noordhoff, the Netherlands, 1994 at pp. 5-10; Dijk, P. van., G.J.H. van Hoof and K. de Vey Mestdag, Supervisory Mechanisms in International Economic Organisations, Kluwer Law and Taxation Publisher, Deventer, the Netherlands, 1984 at 56.

²⁶ The Secretariat of GATT, in fact, was consisted of a handful of staff who actually belonged to the Interim Commission for the ITO [hereinafter referred to as "ICITO"]. Cf. *supra* note 24.

²⁷ Cf. Section 2(a) of the GATT 1994, which demonstrates the proper status of WTO that is based on full legal formalities.

Property. The WTO also provides coverage in Agriculture and in Environment and Sanitary and Phytosanitary measures.²⁸

(3) Unlike GATT, WTO is established firmly on the path towards multilateralism:

The agreements which constitute the WTO are almost all multilateral except, of course, for the "plurilateral agreements" set out in the Annex 4 in the WTO Agreement such as the Codes on government procurement and civil aircraft (formerly also on bovine meat; dairy products).²⁹ WTO involves a series of commitments for all of the signatories. In contrast, the GATT started as a multilateral instrument but then gradually a large number of new agreements which were "plurilateral", were added through various negotiating rounds up to the 1980's. The GATT, therefore, became a "selective" agreement which caused the problem of fragmentation of GATT rules and eventually and paradoxically, ended up undermining the foundations of the GATT.³⁰

(4) In accordance with the new rules and conditions, WTO comes across as a much more sophisticated mechanism than its predecessor GATT:

The WTO dispute settlement system has reputedly gained speed, automaticity, transparency, and a more legalistic approach (rule-oriented) for the solution of problems, as well as a higher degree of effectiveness. The system lays out in much greater detail the procedures to be adopted in the event of a dispute between WTO members; it also sets strict time-scales for the entire dispute settlement procedure³¹

²⁸ For the study on agriculture under GATT, see in general Josling, Timothy E., Tangermann and T.K. Warley, *Agriculture in the GATT*, Macmillan Press Ltd., London, 1996; see for the SPS measures, see *ibid.* at pp. 208-213.

²⁹ See for more information, *supra* note 14.

³⁰ Under the GATT, there appeared to be a problem of complexity because of the interrelationship between the GATT (GATT 1947) and a number of Codes. The Tokyo Round results, for instance, illustrates the point at issue, i.e. as Professor Jackson called, the fragmentation (or "balkanisation") of dispute settlement rules under the various Agreements; for further study in this regard, see Jackson, J.H., "The Birth of the GATT-MTN System: A Constitutional Appraisal", 12 L. Pol'y in Int'l Bus. (1980) at 21, 44.

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and establishes an automatic process for dispute settlement although that process may yet be intercepted by the consensus decision of WTO members, nonetheless, not a consensus in a conventional sense;³² it establishes an Appellate Body (i.e. a second forum) composed of seven persons³³ with demonstrated experience in law, international trade, and the subject matter covered by the agreements in general.

In the meantime, the GATT 1947 remained in force until it expired at the end of 1995.³⁴ This overlap was allowed in order to facilitate the accession to the WTO of all GATT member countries and also to permit the continuation of activities in certain areas, for example, dispute settlement. Furthermore, the GATT 1947 has been amended and up-dated as the "GATT 1994", and as such it has become an integral part of the WTO Agreement.

³¹ The proposed timetable for the working procedures of the panel can be seen in Appendix 3 to the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU).

³² This new consensus is called the "negative consensus" which means that the consensus of objection, namely, a "no" is sought. Further details of the "negative consensus" will be given in the next chapter.

³³ On 29 November 1995, the first appointment of the seven members of the WTO Appellate Body was announced by the WTO Dispute Settlement Body (DSB) and those appointees are as follows: *Mr. James Bacchus* of the United States; *Mr. Christopher Beeby* of New Zealand; *Professor Claus-Dieter Ehlermann* of Germany; *Dr. Said El-Naggar* of Egypt; *Justice Florentino Feliciano* of Philippines; *Mr. Julio Lacarte-Muró* of Uruguay (Chairman); and *Professor Mitsuo Matsushita* of Japan; a detailed profile of appointees can be found in WTO, WTO Focus, No. 6 (October-November 1995) at 8; recently, Mr. C. Beeby has been elected to be the next chairman of the Appellate Body and the term is from 7 February 1998 to 6 February 1999, which was circulated in WT/DSB/11 (5 December 1997), also see Rule 5 of the Working Procedures of Appellate Review, WT/AB/WP/3 (28 February 1997).

³⁴ For the transitional co-existence of the GATT 1947 and the WTO Agreement, see Section 3 of Decision of 8 December 1994 adopted by the Preparatory Committee for the WTO and the CONTRACTING PARTIES to GATT 1947, which states that "*The legal instruments through which the contracting parties apply the GATT 1947 are herewith terminated one year after the date of entry into force of the WTO Agreement. In the light of unforeseen circumstances, the CONTRACTING PARTIES may decide to postpone the date of termination by no more than one year.*"; read in general for the study on transitional period, Marceau, Gabrielle, "Transition from GATT to WTO - A Most Pragmatic Operation", 29 J.W.T. (1995), pp. 147-163.

Chapter 5. THE DISPUTE SETTLEMENT MECHANISM IN WTO (WORLD TRADE ORGANISATION)

"The end of the law is, not to abolish or restrain, but to preserve and enlarge freedom. For in all the states of created beings capable of laws, where there is no law there is no freedom".¹

Introduction

As discussed in Chapters 2 and 3, the "old" dispute settlement mechanism of GATT had defects both in terms of procedure and substance. Therefore, many contracting parties made repeated calls and proposals for improving the mechanism, in particular, at the Uruguay Round of Multilateral Trade Negotiations. Thus, we now turn our attention to the "new" dispute settlement system under WTO, which came into operation on 1 January 1995.² The "new" mechanism brought with it a more legalistic approach to the whole of the procedures and it is based on notions of "effectiveness", "automaticity", and "transparency" in order to eliminate the defects in the dispute settlement mechanism of GATT and ultimately to bring fairness to the world trade system.

Since the new dispute settlement system has come into effect fairly recently, it may be hasty at this stage to assess whether this new dispute settlement system will succeed in bringing about the goals of GATT/WTO. Nonetheless, over one hundred and fifty complaints have already been brought to the WTO since the establishment of the WTO in January 1995.³ This figure is more than half of the total cases which were brought to the GATT Contracting Parties during its life time.⁴ Note that the

¹ Locke, John., Two Treatises of Government, Peter Laslett (ed.), Cambridge University Press, first published 1960, student edition: reprinted 1996, pp. 305-6.

² See for the charts of conflicts brought to WTO, The Financial Times, "Antagonists queue for WTO judgement", 8 August 1996 at 6.

³ 169 requests for consultation were recorded (as of 19 April 1999) (the updated data is available from the WTO homepage on the World Wide Web at [<http://www.wto.org/wto/dispute/bulletin/htm>]; see also for the list of the first 100 disputes brought to the WTO, WTO Focus No. 21 (August 1997).

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popularity of the new system is even spreading to the Members of developing countries who were reluctant to have recourse to the dispute settlement system of the old GATT. For instance, the first dispute brought to the new dispute settlement system of WTO was between two developing countries, Singapore and Malaysia, over the latter's prohibition of imports of polyethylene and polypropylene.⁵ This case became a landmark which established a participation of developing country members in the new dispute settlement mechanism because, as already mentioned, disputes involving only developing countries were very rare under the previous system of GATT. Thus, participation of the developing countries is one of the phenomena of the new dispute settlement system of WTO.

This chapter provides an overview of the WTO dispute settlement mechanism to begin with, then it identifies and compares the "new" dispute settlement procedures of WTO and the "old" system under GATT examined in Chapter 2. This comparison is essential in order to find out whether the defects in the GATT system have been ameliorated under the new WTO system, and if so, in what way.

This chapter therefore will conduct an essential investigation into the new WTO dispute settlement system, which eventually will assist in carrying out case studies in Chapter 7 and 8.

⁴During this period, there were 195 disputes referred to the Contracting Parties, see for the table of those disputes, GATT, Analytical Index: Guide to GATT Law and Practice, Geneva, 6th ed. (1994), at pp. 718-734.

⁵This test case, however, did not reach the "judicial" stage (i.e. panel) of the new procedures. In other words, the disputes was resolved bilaterally through consultation; see The Financial Times, "Neighbours' tiff becomes first WTO case", 23 February 1995 at 4.

5.1. A Beginning of the Multilateral Trade Negotiations: The Uruguay Round⁶

The U.S. idea of a new round of multilateral trade negotiations (i.e. the Uruguay Round) was initially proposed at the Ministerial Conference held in November 1982.⁷ Other governments, however, were reluctant to accept the U.S. proposal. The EC, for instance, showed little enthusiasm for that proposal. The main reason behind its reaction could be explained by the fact a recession was attacking the EC at that time, which further triggered 'Euro-pessimism'. The EC was therefore reluctant to contemplate measures of international trade liberalisation, especially since agriculture and high technology (apart from another important matters such as dispute settlement) were all among the priority issues on the U. S. agenda.

Meanwhile, developing countries objected to the arrangements for a major negotiation just after the Tokyo Round, which was just signed in 1979. They were also opposed to discussing the new trade areas such as services, intellectual property rights, and investment. The inclusion of those areas to GATT deprived the developing countries of the argument that such areas were outside the GATT system. Consequently, the developing countries challenged the legal competence of GATT to handle those new areas, arguing that the original scope of GATT was merely concerned with trade in goods.

In addition to such opposition, there were a number of unaccomplished working programmes which had been made at the Tokyo Round. The EC had proposed to hold a high-level official meeting to plan out the new round, but developing countries blocked a consensus to accept the proposal. The U.S. finally invoked its right to call a Special Session for September 1985.⁸ A number of developing countries such as

⁶ See generally, Hudec, R.H., Enforcing International Trade Law: the Evolution of the Modern GATT Legal System [hereinafter, the "Enforcing"], Butterworths Legal Publishers, U.S., 1993; Pescatore, P., Davey, W. J., Lowenfeld, A.F., Handbook of GATT Dispute Settlement (the new title is: Handbook of WTO/GATT Dispute Settlement [hereinafter, the "Handbook of WTO/GATT"], Transnational Juris Publications, Inc., New York, First released in 1991/ the latest print (Release 8) in June 1997; for the Uruguay Round negotiation history, see in general, Croome, John., Reshaping the World Trade System - A history of the Uruguay Round, World Trade Organisation, Geneva, 1995.

⁷ Ministerial Declaration of 29 November 1982, L/5424, BISD 29S/9 (1983).

⁸ Action taken on 26 November 1985, BISD 32S/12 (1986).

Brazil and India, which had opposed the U.S. action at the beginning, changed their stance by the time the Special Session was held. In any case, the Special Session reached an agreement to create a Senior Official Group to organise the preparatory work necessary for the new round, and the Contracting Parties formally set up a Preparatory Committee to formulate the negotiating agenda.⁹ The Ministers reached a final agreement on the agenda and the UR was finally launched on 20 September 1986 at Punta del Este, Uruguay.¹⁰

The UR was an extremely broad undertaking and wide ranging in the number of subjects it dealt with. The subjects covered thirteen topics including tariffs, non-tariff measures, tropical products, natural resource-based products, textiles and clothing, agriculture, GATT articles, safeguards, MTN Agreements and Arrangements, subsidies and countervailing measures, dispute settlement, TRIPs, and TRIMs.¹¹ Among those subjects listed, particularly the objectives for negotiation with regards to the settlement of disputes were as follows:

In order to ensure prompt and effective resolution of disputes to the benefit of all contracting parties, negotiations shall aim to improve and strengthen the rules and procedures of the dispute settlement process, while recognising the contribution that would be made by more effective and enforceable GATT rules and disciplines. Negotiations shall include the development of adequate arrangements for overseeing and monitoring of the procedures that would facilitate compliance with adopted recommendations.¹²

The NG13 held its first meeting on 6 April 1987. At this meeting, Mr. Lacarte-Muró (Uruguay) and Mr. Katz (United States) were appointed Chairman respectively of the Negotiating Groups on Dispute Settlement and on Functioning of the GATT System.¹³ A number of delegations regarded the dispute settlement mechanism as a

⁹ BISD 32S/9 (1986).

¹⁰ See, Ministerial Declaration on the Uruguay Round, BISD 33S/19-30 (1987).

¹¹ *Ibid.*

¹² See, *ibid.* at 25; also in GATT, GATT Focus, No. 43, January - February 1987, at 6.

¹³ Meeting of 6 April 1987, Note by the Secretariat [hereinafter, the "April 1987 Meeting"], MTN. GNG/NG13/1 (10 April 1987) at 1.

means of securing the fulfilment of GATT obligations. Many delegations, therefore, attached considerable importance to the negotiations in this particular Group. The participants acknowledged that "prompt and effective resolution of disputes was of vital importance for the entire GATT system and to the benefit of all contracting parties."¹⁴ Although the old dispute settlement mechanism functioned reasonably in a number of cases, it had, nevertheless, a number of serious shortcomings or defects since its beginning. Such defects¹⁵ brought a measure of discredit and mistrust with regard to the institutions of the GATT. The participants, therefore, made preliminary proposals for specific subjects to be included in the negotiations such as the following issues:¹⁶

- the nature of dispute settlement;
- the establishment of panels;
- the work of panels;
- the role of the GATT Council;
- the implementation of panel reports;
- equal access to the GATT dispute settlement system; and
- the involvement of third interested parties.

The Chairman, at the end of the discussion on this agenda, insisted on the need for the member states to see the new obligations as beneficial to all:

... the political will necessary for a stricter fulfilment of GATT obligations was unlikely to come about by mere exhortation. There was a need for developing additional incentives and institutional mechanisms encouraging compliance by contracting parties with their GATT obligations which they had voluntarily undertaken in their own national self-interest.¹⁷

¹⁴ *Ibid.*

¹⁵ For the defects in the dispute settlement system in GATT, see at Section 2.3. in Chapter 2 of this thesis.

¹⁶ *Ibid, supra* note 13.

¹⁷ *Ibid.*

This is how the improvement of dispute settlement mechanism became one of the high priority issues for the UR negotiations.

5.2. Dispute Settlement Mechanism of WTO

After the UR negotiations which took over four years for preparation and another seven more years for completion, the UR agreements were finally signed. This section analyses the new dispute settlement mechanism under WTO and further examines the new elements of the new mechanism.

5.2.1. Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiation

"The Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations" (the Final Act), is a lengthy document running to over 550 pages which contains legal texts explaining the results of the negotiations since the beginning of the negotiations which took place at Punta del Este, Uruguay, in September 1986. In addition to the full texts of the agreements, the Final Act also includes the texts of Ministerial Decisions and Declarations which were issued in order to clarify certain provisions of some of the agreements.¹⁸

In the Final Act, the WTO members have pledged themselves to seek recourse to the new dispute settlement system to settle disputes, and to abide by its rules and procedures¹⁹ instead of taking unilateral actions against perceived violations of trade rules as used to be the case during the period of the GATT system. In addition, the Final Act refers to all but two of the negotiating areas cited in the Punta del Este Declaration; the first exception was the result of the "market access negotiations" in which each country has made binding commitments to reduce or eliminate specific

¹⁸ For the chart of the WTO Agreement, see Appendix I to this thesis.

¹⁹ *Infra* note 20, Article 23, para. 1.

tariff and non-tariff barriers to merchandise trade; and the second one being the "initial commitments" on liberalisation of trade in services.

5.2.2. Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU)²⁰

Background:

The Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU) stipulated in Annex 2 to the WTO Agreement emphasises that the prompt and effective settlement of disputes is essential to the effective functioning of the WTO. It sets out in 27 articles totalling 143 paragraphs and four appendices, and a variety of rules intended to achieve a speedy settlement of disputes. In addition, the operation of the DSU is strengthened by rules of conduct designed to maintain the integrity, transparency and confidentiality of proceedings.²¹

In contrast, the dispute settlement provisions of the old GATT were provided for in just two Articles, i.e. XXII and XXIII, though, in an ambiguous expression (the words "dispute settlement" was not explicitly used at all). Hence, the GATT dispute settlement procedures have been built up over the years through the evolution of customary practice, which were later codified in decisions by the contracting parties of GATT - notably the 1979 Understanding and a provisional system, which functioned as interim rules through the end of the UR, and also allowed the 1989 Improvements following the Mid-Term Review of the UR.²² Furthermore, as stipulated in its Preamble, the WTO Agreement clearly stated its intention "to

²⁰ See, Annex 2 "Understanding on Rules and Procedures Governing the Settlement of Disputes" (DSU) in Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations (Marrakesh, 15 April 1994); for the negotiation history of the DSU, see Chapter 3 of the present thesis; see in general, Jackson, J.H., The World Trade Organisation: Constitution and Jurisprudence, Royal Institute of International Affairs, London, 1998, Chapter 4, pp. 59-100.

²¹ See, for Rules of Conduct for the Understanding on Rules and Procedures Governing the Settlement of Disputes, WT/DSB/RC/1 (11 December 1996); for Communication from the Appellate Body concerning the document mentioned, WT/DSB/RC/2 (22 January 1997).

²² For the analysis on the development of the GATT dispute settlement procedures, see at Section 2.5. in Chapter 2 of this thesis.

maintain full continuity with the attainments of the old GATT".²³ Thus, the new WTO system maintained as its source and interpretation of law, those of GATT. In addition, this will of the WTO was also expressed in two operative provisions, namely, Article XVI:1 of the WTO Agreement and Article 3, para. 1 of the DSU respectively.²⁴

The GATT dispute settlement mechanism is considered to be one of the cornerstones of the multilateral world trade order. In fact, although this system had already been strengthened through a number of Understandings and decisions,²⁵ the DSU includes greater automaticity in decisions with respect to the establishment, terms of reference, and composition of panels. "Automaticity" means that decisions no longer require the consent of all member states including the parties to a dispute in order to come into effect. Moreover, the DSU strengthens the existing system significantly, by means of extending the automaticity agreed in the Mid-Term Review to the adoption of the findings of both the panels and Appellate Body. The DSU, moreover, establishes an integrated dispute settlement mechanism which enables WTO members to base their claims on any of the multilateral trade agreements included in the Annexes to the WTO Agreement.²⁶

²³ Pescatore, P., "Drafting and Analysing Decisions on Dispute Settlement", in Pescatore, P., W. J. Davey and A. F. Lawenfeld, *Handbook of WTO/GATT Dispute Settlement*, *supra* note 6, Release 8, June 1997 at 13; see the Preamble to the WTO Agreement which stated "...to develop an integrated, more viable and durable multilateral trading system encompassing the General Agreement on Tariffs and Trade, the results of past trade liberalisation efforts, and all of the results of the Uruguay Round Multilateral Trade Negotiations, ...".

²⁴ See, para. 1, Article XVI of the WTO Agreement states that "... the WTO shall be guided by the decisions, procedures and customary practices followed by the CONTRACTING PARTIES to GATT 1947 and the bodies established in the framework of GATT 1947."; for the same policy in terms of dispute settlement rules, see para. 1, Article 3 of the DSU which defines that "Members affirm their adherence to the principles for the management of disputes heretofore applied under Articles XXII and XXIII of GATT 1947, and the rules and procedures as further elaborated and modified herein."; this section does not handle with this issue extensively but for further reading, see in general, Kuyper, P. J., "The Law of GATT as a special field of International Law - Ignorance, further refinement or self-contained system of international law?", XXV Netherlands Y. B. Int'l L (1994), pp. 227-257.

²⁵ For instance, see at Sections 2.4.1.3.; 2.4.1.5.; 2.4.1.6.; 2.4.1.7. and 2.5.2. in Chapter 2 of this thesis.

²⁶ See, the DSU, *supra* note 20, Article 1, para. 1.

Provisions:

Like the General Agreement, the DSU stresses the importance of consultation (prevention of real disputes) in securing the resolution of disputes at an earlier stage of dispute settlement procedures. It requires a member to enter into consultation procedures within 30 days of a request for consultations from another Member being made.²⁷ If there is no settlement after 60 days from the moment the request for consultations is made, then the complaining party may ask for the establishment of a panel.²⁸ Incidentally, the parties to a dispute may voluntarily agree to undertake alternative means of dispute settlement (i.e. the "diplomatic" means of dispute settlement) such as good offices, conciliation, mediation²⁹ and arbitration.³⁰

If a dispute is not settled through consultations, the parties to the disputes will require the establishment of a panel under the DSU, at the latest, at the meeting of the Dispute Settlement Body (DSB)³¹ following that at which the request first appears as an item on the agenda of the DSB, unless the DSB decides by consensus not to establish a panel (i.e., the "negative consensus" rule)³² at that meeting. This means that a party concerned can refuse once at the first meeting to set up the panel.

The DSU also provides specific rules and deadlines for deciding the terms of reference and the composition of panels. The standard terms of reference³³ will apply

²⁷ *Ibid.*, Article 4, para. 3.

²⁸ *Ibid.*, para. 7.

²⁹ *Ibid.*, Article 5, para. 1; cf. see GATT, para. 1 to 3 of the 1966 Procedures in **BISD 14S/18**, para. 2 and 8 of the Annex to the 1979 Understanding in **BISD 26S/210**, para (1) of the 1982 Ministerial Decision in **BISD 29S/13**, Section D of the 1989 Improvements **BISD 36S/61**.

³⁰ *Ibid.*, Article 25; cf. Arbitration in GATT appeared in Section E, Part I (Negotiations on Trade in Goods) the 1989 Improvements, **L/6489** in **BISD36S/61** at 63.

³¹ "The DSB shall meet as often as necessary to carry out its functions within the time-frames provided in [the DSU]" stipulated in *ibid.*, Article 2, para. 3; in fact, the DSB normally convenes its meeting once a month unless there is an urgent issue to be discussed.

³² *Ibid.*, Article 6, para. 1.

³³ The standard terms of reference of panel is, defined in *ibid.*, Article 7, para. 1, as follows:

"To examine, in the light of the relevant provisions in (name of the covered agreement(s) cited by the parties to the dispute), the matter referred to the DSB by

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unless the parties to the dispute agree to special terms within 20 days of the establishment of the panel.³⁴ In case the parties to the dispute cannot reach an agreement on the panellist (the composition of the panel)³⁵ within the same 20 days, at the request of either party, the DG, in consultation with the Chairman of the DSB and the Chairman of the relevant Council or Committee, shall decide instead.³⁶

Panels normally consist of three persons³⁷ (so far many of the panellist have, in fact, been experienced GATT panels),³⁸ who are independent of the Members, having an appropriate background, normally with wide experience and selected from countries other than from parties to the dispute.³⁹ For that purpose, the Secretariat will maintain an indicative list⁴⁰ of experts of governmental or non-governmental individuals satisfying the criteria.⁴¹

(name of party) in document ... and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in that/those agreement(s)."

³⁴ *Ibid.*

³⁵ According to the Legal Affairs Division of the WTO Secretariat, the time between the establishment of Panel and the composition of Panel is, in average, 5.5 weeks (the interview was carried out in June 1997, at the WTO Secretariat, Geneva).

³⁶ *Ibid.*, Article 8, para. 7.

³⁷ Cf. There were five panel members including two tax experts in one GATT case; see DISC case raised between the EC and the U.S., L/4422 (2 November 1976) in **BISD 23S/98-114** (1997).

³⁸ *Ibid.*, para. 5; according to the information from the WTO Legal Affairs Division, the most popular countries which produce a panellist are mainly small countries such as Hong Kong, New Zealand and Switzerland. This is because that many of disputes involves the Quad and also other big countries, therefore they are eliminated from choice. The most popular person has already been nominated for a panellist for nine time (as of June 1997).

³⁹ *Ibid.*, para. 2 and 3.

⁴⁰ This list includes the roster of non-governmental panellists, which was introduced on 30 November 1984, L/5752 in **BISD 31S/9**.

⁴¹ *Ibid.*, *supra* note 20, Article 8, para. 4; ten people were nominated by the government of Japan as a candidate for a panellist and all of them were accepted by the Secretariat of WTO, see for the list of those panellists, *Nihon Kanzei Kyoukai, Boueki to Kanzei (Trade and Tariff)*, (in Japanese only), June 1996 at 76.

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The details of the panel procedures including a proposed timetable are set out in the Appendix 3 to the DSU.⁴² It states that a panel will normally complete its tasks within six months or, in cases of urgency (not explicitly defined) within three months.⁴³ The period from the establishment of the panel to the circulation of the panel report to the Members *should* not exceed nine months.⁴⁴ The panel reports shall not be considered for adoption by the DSB until 20 days⁴⁵ after the DSB has issued the reports to the Members.⁴⁶ The panel reports will be adopted within 60 days of their issuance (i.e. the date of circulation of a panel report to the Members), unless the DSB decides by consensus not to adopt the report (i.e., the "negative consensus" rule)⁴⁷ or in the case where one of the disputing parties formally notifies the DSB of its intention to file an appeal.⁴⁸

The concept of appellate review is an important new feature of the DSU. Appeals are dealt with by the Appellate Body composed of seven members, three of whom shall serve on any one case.⁴⁹ There are limitations which must be observed, and those are, for example, an appeal must be limited to issues of law covered in the panel report and the legal interpretations made by the panel.⁵⁰ In other words, the facts of the panel report will not be considered at an appeal. Proceedings of an appellate review, as a general rule, *shall* not exceed 60 days from the date a party formally

⁴² *Ibid.*, Article 12 ; for a proposed timetable, see the Appendix 3 (Working Procedures) to the DSU.

⁴³ *Ibid.*, para. 8.

⁴⁴ *Ibid.*, para. 9; cf. The time period of the Appellate Review proceedings, "in no case *shall* ... exceed 90 days" (emphasis added), in *ibid.*, Article 17, para. 5.

⁴⁵ Cf. para. 1 of Section G in the 1989 Dispute Settlement Procedures Improvements, which stated 30 days instead.

⁴⁶ *Ibid.*, Article 16, para. 1.

⁴⁷ Cf. During the GATT time, there was a serious problem at the stage of adoption of panel report. The 1989 Dispute Settlement Procedures Improvements maintained the consensus rule (para. 3 of Section G), see at Section 2.5.2. of this thesis. Though, this rule became a "negative consensus" (rather radical) rule in the DSU at the end of the Uruguay Round.

⁴⁸ *Ibid.*, para. 4.

⁴⁹ *Ibid.*, Article 17, para. 1.

⁵⁰ *Ibid.*, para. 6.

notifies its decision to appeal to the date of the circulation of the Appellate Body report.⁵¹ In the event of delay, the proceedings of any case *shall* not exceed 90 days.⁵² Regarding its competence, the Appellate Body may uphold, modify or reverse the legal findings and conclusions made by the panel.⁵³ The Appellate Body report shall be adopted by the DSB and be unconditionally accepted by the parties to the dispute within 30 days following its circulation to the Members, unless the DSB decides by consensus against its adoption (i.e., the "negative consensus" rule).⁵⁴

Where the panel or the Appellate Body report is adopted by the DSB, the party concerned (the party to the dispute to which the panel or Appellate Body recommendations are directed) shall conform to measures which are inconsistent with the "covered agreements" (i.e. the agreements listed in Appendix 1 to the DSU under Article 1.1 of the DSU) to that recommendation adopted.⁵⁵ If it is impracticable to comply immediately with the recommendations and rulings, the party concerned should be given a reasonable period of time to do so,⁵⁶ the latter to be decided either by an agreement of the parties and an approval by the DSB,⁵⁷ within 45 days of adoption of the report⁵⁸ or through binding arbitration within 90 days after the date of adoption of recommendations and rulings.⁵⁹ In any event, the

⁵¹ *Ibid.*, para. 5, cf. *ibid.*, Article 12, para. 8 and 9; see also *supra* note 44.

⁵² *Ibid.*

⁵³ *Ibid.*, para. 13.

⁵⁴ *Ibid.*, para. 14.

⁵⁵ *Ibid.*, Article 19, para. 1; for the meaning of "covered agreements" in the DSU defined in Article 1.1 of the DSU as "...the agreements limited in Appendix 1 to this Understanding [DSU] (referred to in this Understanding as the "covered agreements")".

⁵⁶ *Ibid.*, Article 21, para. 3; the definition of a "reasonable period of time" is not clear, rather loosely defined.

⁵⁷ *Ibid.*, Article 21, para. 3 (a).

⁵⁸ *Ibid.*, (b).

⁵⁹ *Ibid.*, (c); see also Footnote 12 in *ibid.*, which said that in case the parties cannot reach an agreement on arbitrator within ten days of reference the matter to the arbitration, the Director-General, within ten days after consulting the parties, shall appoint the arbitrator; the first case which referred to the binding arbitration was Japan Alcoholic Beverages case and in this report, the arbitrator (Mr. Julio Lacarte-Muró) finally concluded that a "reasonable period of time" within the meaning of Article 21(3)(c) of the DSU for Japan to implement the recommendations and ruling of the DSU (1 November 1996) is 15 months"; see for the report WT/DS8/15, WT/DS10/15 and WT/DS11/13 (14 February 1997).

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DSB shall retain control over the implementation of recommendations or rulings under regular surveillance until the issue is resolved.⁶⁰

Further provisions of the DSU set out rules for remedies, i.e. compensation or the suspension of concessions, in case of non-implementation. Within a specified time-frame ("a reasonable period of time") determined pursuant to paragraph 3 of Article 21, the party concerned who fails to comply with the panel's decision can enter into negotiations with any party having invoked the dispute settlement procedures, so as to arrive at a mutually acceptable compensation.⁶¹ If this has not been the case, then, a party to the dispute may request authorisation from the DSB to suspend concessions or other obligations (i.e. retaliation) provided for in the covered agreements.⁶² The DSB shall grant such authorisation to suspend concessions or other obligations within 30 days of the expiry of the agreed time-frame for the implementation unless the DSB decides by consensus to reject the request (i.e., the "negative consensus" rule).⁶³ Disagreements over the level of proposed suspension will be referred to arbitration.⁶⁴ As a general principle,⁶⁵ concessions should be suspended, to begin with, in the same sector as that in issue in the panel case (where the panel or Appellate Body has found a violation or other nullification or impairment).⁶⁶ Second, if this is not practicable or effective, the suspension can be made in a different sector under the same agreement.⁶⁷ Third, if this is not practicable or effective and if the circumstances are serious enough, the suspension of concessions may be made under another covered agreement.⁶⁸

⁶⁰ *Ibid.*, para. 6.

⁶¹ *Ibid.*, Article 22, para. 2.

⁶² *Ibid.*

⁶³ *Ibid.*, para. 6.

⁶⁴ *Ibid.*, see Recourse to Arbitration by the European Communities Under Article 22.6 of the DSU (Decision by the Arbitrators), WT/DS/ARB (9 April 1999).

⁶⁵ The new principles for suspension of obligation, called "cross-sectoral-retaliation" is defined in *ibid.*, Article 22, para. 3 (a), (b) and (c).

⁶⁶ *Ibid.*, para. 3 (a).

⁶⁷ *Ibid.*, (b).

⁶⁸ *Ibid.*, (c).

Furthermore, the DSU contains a number of special provisions devised for cases which involve the developing and the least-developed countries.⁶⁹ For example, with respect to dispute settlement cases in which a least-developed country member is involved, if no satisfactory solution is found during consultations, the DG or the Chairman of the DSB will, upon request by the less-developed country member, offer their good offices, conciliation and mediation before a request for a panel is made.⁷⁰

The DSU further stipulated certain issues which were not stated in detail under the old GATT rules. For example, a set of special rules for the resolution of disputes which involve non-violation complaints are set out in Paragraph 1(b) of Article XXIII of GATT 1994.⁷¹ In addition to that provision, the DSU provides for a separate article particularly dealing with non-violation complaints in paragraph 1 of Article 26 of the DSU.⁷²

First of all, regarding the issue of burden of proof, in contrast to violation cases where the respondent shall rebut the accusation,⁷³ the complainant shall present a

⁶⁹For details for special procedures involving Least-Developed Country Members, *ibid.*, *supra* note 20, Article 24; these for involving Developing Country, *ibid.*, Article 3:12; 4:10; 8:10; 12:10 and 11; 21:2, 7, and 8; and 27:2; see also the Decision of 5 April 1986 (BISD14S/18).

⁷⁰*Ibid.*, para. 2.

⁷¹For details, see *ibid.*, Article 26.

⁷²During the past GATT time, a non-violation was unpopular partly due to its strict legal burden of proof which was born by the claimant. The claimant therefore raised this type of claim as a secondary (or alternative to a violation claim) claim. Furthermore, in practice, the panel did not examine such claim because it normally found a violation in the principle claim (violation claim). Accordingly, based on the GATT customary practice of the panel, the secondary claim (non-violation claim) was not examined. Nonetheless, there are three cases adopted (or settled) panel decision based on a non-violation claim: (i) Australian Subsidy on Ammonium Sulphate (adopted 3 March 1955) (BISD II/188-196), settled bilaterally between the parties concerned and notified the CPs on 6 Nov. 1950 (GATT/CP.5/SR.6); (ii) Treatment by German Import of Sardines (BISD 1S/53-59), the report was adopted on 31 Oct. 1952 (SR.7/12); and (iii) EEC - Payments and Subsidies Paid to Processors and Producers of Oilseeds and Related Animal-Feed Proteins (BISD 37S/86-132), the report was adopted on 25 January 1990 (C/M/238). Cf. This article also extensively defines cases involving a complaints of the type described in para. 1(c) of Article XXIII of GATT 1994, known as "situation complaints".

⁷³*Ibid.*, Article 3, para. 8.

detailed argument to support a case of non-violation complaint.⁷⁴

Second, since no violation of WTO rules has been established, there is no obligation to withdraw the measure challenged due to nullification or impairment of benefits, or impediment to the attainment of objectives⁷⁵ as opposed to violation cases where the first objective is usually to secure the withdrawal of the inconsistent measures at issue.⁷⁶

Accordingly, in non-violation cases, the party concerned moves onto to the second alternative, that is, compensation (which is usually available in violation cases).⁷⁷ Nonetheless, the coverage of compensation in non-violation cases is broader than basic compensation. In other words, the Member concerned make a "mutually satisfactory adjustment"⁷⁸ which could be equated with a "solution mutually acceptable"⁷⁹ defined as the ultimate aim, namely, securing a positive solution, of dispute settlement mechanism taking into account the findings by the panel or Appellate Body. In addition, that "adjustment" could includes a withdrawal of the offending measures, though not obligatory in non-violation claims, and which also may be in final settlement of the dispute.⁸⁰

On the other hand, the DSU explicitly states in Article 26:1(d) that compensation, though temporary and voluntary,⁸¹ "may be a part of a mutually satisfactory adjustment" as a final settlement of dispute. Whatever a settlement is drawn within the sense of "mutually satisfactory adjustment",⁸² this settlement must be accepted by both parties.

⁷⁴ *Ibid.*, Article 26, para. 1 (a).

⁷⁵ *Ibid.*, para. 1 (b).

⁷⁶ See for the general principle of remedies (in hierarchical order, *ibid.*, Article 3, para. 7: (i) Withdrawal of measures concerned; (ii) Compensation (as a temporary measure); (iii) Retaliation (as the last resort).

⁷⁷ *Ibid.*

⁷⁸ *Ibid.*, Article 26, para. 1 (b).

⁷⁹ *Ibid.*, *supra* note 76.

⁸⁰ *Ibid.*, Article 26, para. 1 (d).

⁸¹ *Ibid.*, Article 22.

⁸² An additional important point in connection with "mutually satisfactory adjustment" in

Arbitration may offer suggestions, though non-binding, with respect to the level of benefits nullified or impaired, and also ways and means of reaching a mutually satisfactory adjustment.⁸³ In case the disputing parties cannot reach any agreement upon such adjustment, retaliation (i.e. suspending the application of concessions or the other obligations) remains available as a last resort.

The last point to be pointed out is that regarding the enforcement procedures for panel and Appellate Body reports in the case of non-violation claims, there is no difference between violation and non-violation cases, except two points in respect of the latter, that is, (i) no obligation is required to withdraw the measures at issue,⁸⁴ and (ii) arbitration, as an additional means to arrive at a settlement, is available.⁸⁵

Finally, as briefly mentioned earlier, the special procedures for a dispute which involves least-developed country members is stipulated in Article 24 of the DSU. Furthermore, in the light of the special forum available to those members,⁸⁶ the WTO Secretariat is required, for instance to assist panels (on the legal; historical and procedural aspect of the matters at issue), and provide secretarial and technical support. In addition, the Secretariat, at the parties request, may provide additional legal advice and assistance regarding dispute settlement to developing country

Article 26:1 (b) should be mentioned, which is that the idea of this phrase could not be considered separately from "consultation" (non-judicial approach and an initial means of settlement in the whole dispute settlement system) once all judicial procedures have been exhausted. In short, even though disputes are reached to the judicial settlement (i.e. panel) stage of the system, an option of non-judicial settlement still co-exists, in other words, always available without intermission. This situation demonstrates a key feature, that is, continuity of non-judicial character of the new dispute settlement mechanism of WTO, which has been inherited from the former GATT system (cf. Article 3.1 of the DSU; Article XVI:1 and the Preamble to the WTO Agreement), i.e. a clear preference of non-judicial settlement of disputes concurrent with panel proceedings (judicial means of dispute settlement). In other words, despite the progressive rules are provided in the new dispute settlement system of WTO, the spirit of the old GATT dispute settlement system still lies at the core as a fundamental element in WTO. This fact may give us a clue in understanding the new dispute settlement mechanism

⁸³ *Ibid.*, Article 26, para. 1 (c).

⁸⁴ *Ibid.*, (b).

⁸⁵ *Ibid.*, (c).

⁸⁶ *Ibid.*, Article 27.

Members. For those purposes, the Secretariat shall offer a qualified legal expert⁸⁷ (with impartial capacity) from the technical co-operation services of the WTO. Furthermore, the Secretariat shall run special training courses⁸⁸ for Members who are interested in procedures and practices of dispute settlement mechanism.

5.3. Major Technical Innovations in the New Dispute Settlement Mechanism

This section will highlight the major technical innovations in the DSU. Although the procedures are, in principle, based on the old dispute settlement mechanism of GATT (including its drafting history, customary practice, and old decisions),⁸⁹ they brought a number of new elements into the system, such as: (i) Automaticity, (ii) the Appellate Body, (iii) Cross (Sectoral) Retaliation, (iv) Transparency, (v) Restriction against Unilateral Measures. Each of these elements are examined in turn.

(i) Automaticity

The DSU states that "*The dispute settlement system of the WTO is a central element in providing security and predictability to the multilateral trading system*".⁹⁰ Furthermore, the DSU emphasises that prompt settlement of disputes is essential to the effective functioning of the WTO.⁹¹ In this regard, the new procedures establishes a new body, what is called the Dispute Settlement Body (DSB) which is convened by the General Council⁹² and deals with all disputes arising from any

⁸⁷The Secretariat of WTO provides two legal advisors for this purpose set out in Article 27, para. 2 of the DSU, and those are, as of August 1997: Professor Ernst-Ulrich Petersmann and Professor Petros C. Mavroidis. Both are ex-Secretariat official of GATT/WTO.

⁸⁸For example, the Legal Affairs Division of the WTO Secretariat offers courses on dispute settlement mechanism for the Members upon their request. There are two different length of course: a short course (for a few days) and a long course (for several days).

⁸⁹Cf. *ibid.*, *supra* note 20, Article 3, para. 1 "adherence to the principles ... under Articles XXII and XXIII of GATT 1947"; also see, Article XVI.1 of the WTO Agreement and the Preamble to the WTO Agreement.

⁹⁰*Ibid.*, *supra* note 20, Article 3, para. 2.

⁹¹See, *ibid.*, para. 3.

⁹²Marrakesh Agreement Establishing the World Trade Organisation (the WTO

agreement contained in the Final Act. The DSB replaces the General Council in making decisions on the establishment of panels, the adoption of panel and appellate body reports and authorises suspension of concessions and other obligations provided for in the covered agreements.⁹³

Two main devices strengthen the automaticity element of the panel procedures. First, the "Negative Consensus" rule which means that the panel procedures will proceed if, at least, one country approves of a decision. Accordingly, parties to the dispute in the new system can no longer block the establishment of panels or the adoption of panel reports as used to be the case under the old system under GATT. This new rule is applied to several stages of the procedures: (a) establishment of panels;⁹⁴ (b) adoption of panel reports;⁹⁵ (c) adoption of Appellate Body report;⁹⁶ (d) the DSB's authorisation of retaliatory measures for failure to implement recommendations within 30 days of the expiry of the reasonable period of time;⁹⁷ and (e) the DSB's authorisation of retaliatory measures (i.e. suspension of concessions or other obligations).⁹⁸

Second, detailed and strict time frames for each stage of procedure have been incorporated.⁹⁹ For example, the establishment of a panel is almost automatic.

Agreement, Appendix 2 of this thesis, Article IV, para. 3; cf. the original proposal of the DSB was made by the Hong Kong delegation, see at Section 3.2 in Chapter 3 of this thesis at 11.

⁹³ *Ibid.*, *supra* note 20, Article 2, para. 1.

⁹⁴ *Ibid.*, Article 6, para. 1.

⁹⁵ *Ibid.*, Article 16, para. 4; cf. para. 3 of Section G in the 1989 Dispute Settlement Procedures Improvements (served tentatively through the Uruguay Round), which states "The practice of adopting panel reports by consensus shall be continued...".

⁹⁶ *Ibid.*, Article 17, para. 14.

⁹⁷ *Ibid.*, Article 22, para. 6.

⁹⁸ *Ibid.*, para. 7.

⁹⁹ The time period can be found in various numbers of provisions in the DSU, for instance;

Consultation: DSU (Article/paragraph) 4.3, 4.7, 4.8, 4.11, 12.10; Conciliation: DSU 5; Developing Countries: DSU 3.12, 12.10; Duration - Appellate Body Process: DSU 17.5, 20, 21.4, and Panel Process: DSU 12.8, 12.9, 12.10, 20, 21.4; Extension of Time Limit - Appellate Body: DSU 17.5, 20, 21.4, and Panel: DSU 12.9, 12.10, 20, 21.4; Frequent Meetings of the DSB: DSU 2.3; Implementation: DSU 21.3, 21.4; Multiple Complaints: DSU 9.3; Non-Violation Complaints: DSU 26.2 [also in Montreal Decision Section G(4)];

Under the new system, if the countries involved do not respond to a request for consultations within 10 days after the date of receipt of the request for consultations,¹⁰⁰ or do not enter into consultation within a period of no more than 30 days,¹⁰¹ or if the consultations fail to reach a solution within 60 days after the date of receipt of the request for consultation,¹⁰² the complainant may ask the DSB to establish a panel. In addition, panel reports must be adopted, as a general rule, within nine months, or twelve months in the case of an appeal.¹⁰³

(ii) Appellate Body¹⁰⁴

The establishment of the Appellate Body is also one of the most notable innovations introduced by the Final Act. This new attribute of the WTO dispute settlement mechanism provides all the parties to a dispute with the opportunity to appeal against a panel proceeding.¹⁰⁵ The Appellate Body, as a tribunal of second instance, examines only the legal aspects of the panel report whenever one of the parties to the disputes is dissatisfied with its findings. Any appeal, however, must be limited to

Panel Procedures: DSU 12.2, 12.3, 12.4, 12.6, Appendix 3.12; Reasonable Period of Time for Implementation: DSU 21.3, 23.2(c); Suspension of Procedures: DSU 12.12; Urgency - Consultations: DSU 4.8 and Generally: DSU 4.9 and Panel Process of Duration: DSU 12.8 and Production of Panel Reports: DSU 12.8, 12.9.

¹⁰⁰ *Ibid.*, Article 4, para. 3.

¹⁰¹ *Ibid.*

¹⁰² *Ibid.*, para. 7.

¹⁰³ *Ibid.*, Article 20.

¹⁰⁴ *Ibid.*, Article 17.

¹⁰⁵ A first Notice of Appeal made by the United States, see WTO, WTO Focus, No. 8 (January-February 1996) pp. 1-3; for the Appellate Body's Working Procedures for Appellate Review which came into effect on 15 February 1996, see WT/AB/WP1 (15 February 1996), which was later replaced by WT/AB/WP/3 (27 February 1997); the first appeal under this new system was made by the United States over the Panel Report, the United States - Standards for reformulated and Conventional Gasoline, WT/DS2/R (29 January 1996). In this appeal, the United States (appellant), Brazil and Venezuela (appellees), and the European Communities and Norway (third participants) were involved. For the official report of the Appellate Body of this first appeal, see WT/DS2/AB/R (29 April 1996). According to the data prepared by the WTO Secretaria, eighteen cases were brought to the AB so far (as of 18 April 1999); for the Dispute Settlement Overview (which includes the latest summary of WTO dispute settlement activities and all panel and appellate reports of the WTO) can be found on the WTO's homepage on the World Wide Web at [<http://www.wto.org/wto/dispute/bulletin.htm>] (available since 26 September 1995).

issues of law covered in the panel report and the legal interpretation developed by the panel.¹⁰⁶

The Appellate Body consists of seven persons who are appointed¹⁰⁷ for four-year terms renewable once.¹⁰⁸ Three of them will serve on any one case by rotation. They must be persons recognised as authorities in the field and independent of any government.¹⁰⁹ The total work period of the Appellate Body must be completed in 60 days, or exceptionally 90 days after the notification of the intention of appeal to the Appellate Body.¹¹⁰ In addition, all proceedings of the Appellate Body must be confidential.¹¹¹ The Appellate Body, in consultation with the Chairman of the DSB and the DG of the WTO, must draw up working procedures.¹¹² Finally, the Appellate Body may uphold, modify or reverse the legal findings and conclusions of the Panel.¹¹³

(iii) Cross (Sectoral) Retaliation¹¹⁴

¹⁰⁶ *Ibid.*, *supra* note 104, para. 6.

¹⁰⁷ See for the list of the first seven members for the appellate body, Footnote 33 in Chapter 4 of this thesis.

¹⁰⁸ Recently, pursuant to the provisions of Article 17.2 of the DSU, three appellate body members were reappointed for a final term of four years. Those three members selected by lot were: Mr. Claus-Dieter Ehlermann, Mr. Florentino P. Feliciano and Mr. Julio Lacarte-Muró, see *WT/DSB/M/35* (18 July 1997) at 7. Accordingly, the term of those three members will be until December 2001, and which is unrenovable.

¹⁰⁹ *Ibid.*, *supra* note 104, para. 3.

¹¹⁰ *Ibid.*, para. 5.

¹¹¹ *Ibid.*, para. 10.

¹¹² *Ibid.*, para. 9; also see Working Procedures of Appellate Body Review, *WT/AB/WP/3* (28 February 1997) which is a consolidated version of the Working Procedures for Appellate Review, and replaced *WT/AB/WP/1* (15 February 1996).

¹¹³ *Ibid.*, para. 13; no case has been yet reversed as of December 1997; the first case in which the AB has totally reversed the conclusion of Panel was the EC - Customs Classification of Certain Computer Equipment (LAN) case (brought by the US), *WT/DS 62, 67, 68/AB* (5 June 1998).

¹¹⁴ Cf. *Brazil v United States: Import Restrictions on Certain Products from Brazil ["Pharmaceuticals" Retaliation]* (24 August 1988) for further information Hudec, R. E., *The Enforcing*, *supra* note 6, at 571.

Unlike the previous mechanism under GATT, the new dispute settlement mechanism is an integrated one which means that the DSU applies to disputes arising from: (a) the WTO Agreement (the Agreement Establishing the World Trade Organisation); (b) the MTAs (Multilateral Trade Agreements) such as: Annex 1A: Multilateral Agreements on Trade in Goods (GATT 1994); Annex 1B: GATS (General Agreement on Trade in Services); Annex 1C: TRIPs (Agreement on Trade-Related Aspects of Intellectual Property Rights); and, Annex 2: DSU (Understanding on Rules and Procedures Governing the Settlement of Disputes); (c) the PTAs (the Plurilateral Trade Agreements) (each of the agreements applies only to signatories) such as: Annex 4: Agreement on Trade in Civil Aircraft; Agreement on Government Procurement; International Dairy Agreement;¹¹⁵ and, International Bovine Meat Agreement.¹¹⁶ Retaliation, in principle, shall be initiated in the same sector in which the dispute occurs.¹¹⁷ If this retaliation is considered impracticable or ineffective, retaliation shall take place in other sectors under the same agreement.¹¹⁸ If this turns out to be impracticable or ineffective also, retaliation could take place in another covered agreement mentioned earlier on.¹¹⁹

If a country concerned disagrees with the level of suspension proposed, or claims that the principles and procedures stipulated in Article 22, para. 3 (b) or (c) of the DSU have not been followed, the matter shall be referred to arbitration.¹²⁰

(iv) Transparency

The new dispute settlement mechanism contains a number of rules intended to bring more transparency to its procedures.¹²¹ For instance, a party to a dispute is not

¹¹⁵ This agreement was terminated at the end of 1997; see Press/78 (30 September 1997).

¹¹⁶ This agreement was also terminated at the same time, see *ibid.*

¹¹⁷ *Ibid.*, Article 22, para. 3(a).

¹¹⁸ *Ibid.*, para. 3(b).

¹¹⁹ See, Appendix 1 to the DSU; also, *ibid.*, para. 3(c).

¹²⁰ *Ibid.*, para. 6.

¹²¹ *Ibid.*, Appendix 3, para. 10 which states that "In the interest of full transparency, the presentations, rebuttals and statements [submitted during the 1st and 2nd meetings] shall be

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prevented from disclosing statements of its own positions to the public.¹²² Moreover, a party to a dispute, upon a request of other members, may disclose to the public a non-confidential summary of the opinion papers submitted during the panel proceedings.¹²³ Another example is found in one of the tasks of WTO, namely, the task of surveillance in relation to implementation of recommendations and rulings,¹²⁴ and to compensation and the suspension of concessions.¹²⁵

Furthermore, the WTO's TPRM (Annex 3 to the WTO Agreement), basing itself upon the 1979 Understanding, can also be regarded as an indication of the WTO procedure achieving greater transparency.¹²⁶ The objectives of this mechanism are: to examine the impact of each Member state's trade policy and practice on the multilateral trading system; and to contribute to improve adherence by all Member states to WTO rules (i.e. rules, disciplines, and commitments made under the MTAs and, where applicable, the PTAs) by accomplishing greater transparency. While this mechanism functions effectively in preventing potential disputes concerning trade policies or practices of Member states by requirements, such as submission of periodic reports on their trade policies.¹²⁷

Finally, one more feature relating to the new WTO dispute settlement system, which demonstrates greater transparency, should be pointed out. This is derestriction of panel reports under the WTO system. As discussed in the earlier chapter, under the old GATT practice, panel reports were classified as restricted documents and only became available to the public after acquiring the consensus to adopt them, by the

made in the presence of the parties. Moreover, each party's written submissions, including any comments on the descriptive part of the report and responses to questions put by the panel, shall be made available to the other party or parties".

¹²² *Ibid.*, Article 18, para. 2.

¹²³ *Ibid.*

¹²⁴ *Ibid.*, Article 21, para. 6.

¹²⁵ *Ibid.*, Article 22, para. 8.

¹²⁶ Annex 3 (Trade Policy Review Mechanism) to the WTO Agreement.

¹²⁷ See, Annex 3, *ibid.*, and also see at Footnote 12 in Chapter 4 of the thesis.

GATT Council. It, however, often took some time before the reports were circulated to the public, i.e. printed in the BISD under the subject heading of "Conciliation". Furthermore, in the event of a panel report being unadopted by the Council, that report remained as a restricted document and, in principle, never became available to the public. The General Council of WTO decided to treat panel reports as derestricted documents but providing that a party can request restricted status for up to ten days.¹²⁸ In addition, the rest of the documents issued as the "WT/DS/..." series will be derestricted documents unless a party concerned requests a restricted status. In the meantime, however, the minutes of DSB meeting will remain restricted for six months.¹²⁹

(v) Restrictions Against Unilateral Measures

The issue of unilateral measures was one of the most contentious issues throughout the UR negotiations. It has been a central issue especially between the U.S., the EC and Japan among others. In fact, it was the EC which had originally brought the issue to the negotiations round. Moreover, it must be noted that, as touched upon in Chapter 3, Japan was also one of the initiators regarding the prohibition of unilateral actions, particularly targeting that of the U.S. under the Section 301. Japan made this point on various occasions. What happened was that, up until the end of the negotiations in the UR, the U.S. had opposed a particular proposal which was referred to in Chairman's (Mr. Lacarte) proposal to the DG, Mr. Dunkel: that all Members should undertake to refrain from using unilateral measures to settle disputes;¹³⁰ and should bring their legislations into conformity with the dispute settlement procedures of GATT. Finally, the U.S. managed to maintain its position

¹²⁸ This WTO General Council decision was made on 18 July 1996, see WT/L/160.

¹²⁹ See at para. (c) of the Appendix in WT/L/160/Rev. 1 (26 July 1996) at 3.

¹³⁰ Article 23, para. 1 of the DSU states that the Members shall have recourse to, and abide by, the rules and procedures of the DSU; *ibid.*, para. 2 also provides that the Members shall not make a determination of violation of WTO itself except through the rules and procedures of the DSU.

that each member's legislations are not required to conform to the GATT dispute settlement procedures.

As mentioned earlier, the multilateral dispute settlement system has been undermined partly because of unilateral measures, namely, the controversial Section 301 of U. S. trade law. The United States tends to rely upon unilateral measures as an instrument in resolving trade disputes with other Member states in spite of some doubt over compatibility with the multilateral approach under the new system of WTO.¹³¹

U.S. behaviour was partly propelled because of the vacuum that then existed under the old GATT system (e.g. the limits of jurisdiction under GATT). The old system did indeed furnish the U. S. with a number of opportunities to disguise their unilateral policies. First, for example, unlike the WTO Agreement, the GATT rule did not cover certain areas (presently known as a "new area" which are covered by the WTO Agreement) such as services and intellectual property. Nonetheless, the importance of services and intellectual property lies as an ever-increasing part of the industrialised countries' trade.¹³² Accordingly, the conflict between the industrialised and industrialising countries over the new area (e.g., high-technology industries) has intensified. Another reason for the U. S. policy of unilateral measures could be explained by the fact that there were systemic defects of the GATT system due to its unfortunate *de facto* origin. For instance, "consensus" (including parties to a dispute) requirement which had been used over decades under the GATT system, was necessary for the adoption of panel reports or for approval of retaliation. Such traditional and stringent requirements, however, often caused delay in dispute

¹³¹ "...the United States often threatens sanctions and actually takes retaliatory actions to coerce the target country into changing the trade law or practice at issue", see Industrial Structure Council, 1994 Report on Unfair Trade Policies - by Major Trading Parties, Research Institute of International Trade and Industry Publication Department, Tokyo, Japan, 1994 at 236.

¹³² "By the late 1970s, services in the United States accounted for two-thirds of the GNP and for more than 50 percent of the GNPs in twelve other developed countries" and "By 1986, for example U.S. exports of services amounted to \$148.4 billion, equivalent to 39.8 percent of U.S. exports" in Spero, Joan Edelman., The Politics of International Economic Relations, 4th ed., Routledge, U.K., 1990 (Reprinted in 1992 and 1993), at 90; see in general for the issue of services and intellectual property, *ibid.*, 90-91 and Gilpin, Robert., The Political Economy of International Relations, Princeton University Press, Princeton, New Jersey, 1987, at pp. 201-203.

settlement procedures. In fact, that rule was even misused by some countries (mainly by the U.S. and the EC).

After such experiences during the GATT period, the new dispute settlement procedures have installed "automaticity" in the procedures by introducing the negative consensus rule.¹³³ In addition, the new procedures considerably restrain such unilateral measures by explicitly stating that WTO dispute settlement procedures must be used in order to recover damages caused by violations prohibited in the WTO Agreement.¹³⁴ According to the WTO, the use of "Section 301" is now closely tied to multilateral dispute settlement, at least for WTO members and in areas subject to WTO rules and disciplines.¹³⁵ Nevertheless, there still exists a certain possibility for the U. S. to use unilateral action as long as such action meets with the requirements defined in the WTO Agreement including the DSU.¹³⁶ This issue is examined in the following section.

5.4. Emerging Issues in the New Dispute Settlement Mechanism

This section raises several issues which one should be aware of under the evolutionary dispute settlement system of WTO.

¹³³ For provisions which apply a negative consensus rule, see under (i) Automaticity in Section 5.3. (Major Technical Innovations in the New Dispute Settlement Mechanism) of this chapter.

¹³⁴ See, *ibid.*, *supra* note 20, Article 23, para. 1 which aims at strengthening the Multilateral System and therefore defined an obligation to have recourse to and abide by, the rules and procedures provided for in the DSU when Members seek to redress a violations or other nullification or impairment of benefits under the covered agreements (listed under Appendix 1 to the DSU) or an impediment to the attainment of any objectives of those agreements.

¹³⁵ See, PRESS/TPRB/46 (31 October 1996) at 7.

¹³⁶ Professor Jackson argued in his article that "There may need to be some alterations to some time limits, or transition measures, but the basic structure of 301 is not necessarily inconsistent with the Uruguay Round results. Section 301 when appropriately used in its current statutory form can be a constructive measure for U. S. trade policy and for world trade policy". Possible cases where the U. S. may resort to such measures will be mentioned in Section 5.2.4. of this chapter, see Jackson, John H., "The World Trade Organisation, Dispute Settlement, and Codes of Conduct", in Collins, Susan M., and Barry P. Bosworth (eds.), The New GATT: Implications for the United States, The Brookings Institution, Washington D. C., 1994, at 74.

(i) Unilateral Measures

The WTO Agreement states that the Members have agreed to use the rules and procedure of the multilateral system of WTO. Furthermore, the DSU stipulates that the WTO member shall use the rules and procedures set forth in the DSU when a WTO member seeks a redress for a breach of obligations in covered agreements, or of an impediment to the attaining of any objective under the covered agreements.¹³⁷ In that sense, the WTO helps to narrow down the scope of unilateral actions by any Member state than used to be the case.¹³⁸

Nonetheless, even with the strengthened and wider-scope coverage of the WTO system, the U. S. might still have some possibility of exercising its unilateral measures, i.e. Section 301 of the Trade Act of 1974, amended by the Omnibus Trade and Competitiveness Act of 1988. How could the U. S. recourse to its unilateral measures be confirmed within the new WTO system? The U. S. may have access to the measures within the framework of the new rules. In principle, the following would be the case:

-the U. S. may take unilateral measures based on Section 301 because no provision of the WTO Agreement refers to the abolishment of the U.S. Section 301;

¹³⁷ *Ibid.*, Appendix 1, *supra* note 119.

¹³⁸ In fact, there are a few countries which have unilateral measures. Nonetheless, the U.S. is the only country which often recourse to such actions. In the meantime, while the E.C. also has such measures, i.e. (Regulation 2461/84 OJ L252, 20.9.84) which is better known as the "new instruments" and the EC's main purpose is not for a regular usage but for countermeasure to the unilateral actions by the other state, most likely the U.S. In addition, their measures are narrower in scope than the U.S. Section 301; EC producers made six complaints until 1993 under the instruments brought. For a further study on the relationship between the instruments and the use of the GATT dispute settlement system, see Petersmann, E.-U., "The GATT Dispute Settlement System as an Instrument of the Foreign Trade Policy of the EC", in Emiliou, Nicholas. and David O'Keeffe (ed.), The European Union and World Trade Law: After the GATT Uruguay Round, John Wiley & Sons, Chichester, England, 1996 at 269-272; for an overview of the EC regulation, see Schoneveld, Frank., "The European Community Reaction to the "Illicit" Commercial Trade Practices of Other Countries", 26 J. W. T., No. 2 (April 1992), pp. 17-34; see for the current development of the instruments and the new EC regulation, Bronkers, Marco.C.E.J., "Private Participation in the Enforcement of WTO Law: The New EC Trade Barriers Regulation", 33 C.M.L.Rev. (1996), pp. 299-318.

-under WTO, the U. S. is still free to have recourse to unilateral actions based on Section 301 against non-members of WTO; and,

-regarding an infringement of bilateral agreements, if the alleged violation takes place outside of the WTO agreement, and as long as retaliatory actions taken under Section 301 do not violate any rights of the opposing party protected under the WTO agreement, then the U. S. would be free to take action.

As stated in the DSU,¹³⁹ it applies to disputes which fall within the scope of the covered Agreement.¹⁴⁰ Although unilateral action remains available in some cases, as explained above, it is true that an initial step toward an ending of any unilateral action is, at least, discernible.

(ii) Negative Consensus Rule

This new consensus principle requires, at least, one member's agreement to a decision. As explained earlier, the negative consensus method will be used at different phases in the settlement process of dispute.¹⁴¹ In one sense, it seems that this rule could be considerably useful and effective to speed up the dispute settlement process. On the other hand, however, it could be a quite hazardous rule at the same time. For example, the negative consensus means that just one member state agrees to the adoption of a panel report, then it will simply be adopted. Namely, a winning party, in all likelihood, will approve of the adoption of a panel report. In this respect, a crucial element is the selection of panellists who drafted a panel report in the

¹³⁹ Article 1, para. 1 of the DSU.

¹⁴⁰ Appendix 1 to the DSU.

¹⁴¹ See, (i) Automaticity in Section 5.3. of this chapter and those stages are: (1) the establishment of panels in DSU Article 6.1, (2) the adoption of a panel report in DSU Article 16.4, (3) the adoption of an appellate report in DSU Article 17.14, (4) the DSB authorisation of retaliation (to suspend concessions or other obligations) in case the member in breach has failed to implement the relevant rulings and recommendations within 30 days of the expiry of the reasonable period of time in DSU Article 22.6, (5) the DSB authorisation to suspend concessions or other obligations where the request is consistent with the arbitrator's decision in DSU Article 22.

dispute settlement process since they could influence a final decision when they draft a report of each case. Notwithstanding, despite its unacceptable behaviour in terms of smooth operation of the procedure, a defeated county could impede the adoption of a panel report under the previous GATT system. What a party in dispute should be concerned with is the quality of individual panellist under the new system since a panellist reserves the right to make recommendations or rulings over an issue in dispute. In short, extra attention is necessary at the early stage of the panel proceedings.

(iii) The Appellate Body

As mentioned, the Appellate Body is a new creation of WTO.¹⁴² The Appellate Body report is to be almost automatically adopted by the DSB and unconditionally accepted by the parties to the dispute unless there is a consensus against its adoption. Therefore, issues concerning the individual quality of panellists and also the background of the each member of the Appellate Body will be crucial factors in the new system.

The background of appellate judges varies from diplomatic experience, academic career, to a judicial background. The diverse background of the judges may bear upon his or her opinion in an appeal. Furthermore, due to the various backgrounds of members of the Appellate Body, the way of drafting a report differs.¹⁴³ In practice, therefore, in order to maintain uniformity of reports, once three appellate judges appointed (in an action) complete their draft of an appellate report, all seven appellate judges make a practice of convening at the WTO Secretariat in Geneva to have further discussions about the arguments presented in the draft report and to exchange individual opinions taking into account extensive and often exhaustive group analysis to produce a final draft as an appellate report.¹⁴⁴

¹⁴²For the Appellate Body, see at Section 5.3. (ii) of this thesis; *ibid.*, Article 17, *supra* note 104; WT/AB/WP/3, *supra* note 105.

¹⁴³This information was given during the interview with a member of the Appellate Body (May 1997, Geneva); see Pescatore, P., "Drafting and Analysing Decisions on Dispute Settlement", *supra* note 6, pp. 42-46.

One may argue that the disputing parties are frequently likely to appeal the panel decision simply because of the availability of the second forum. Furthermore, if appeals happen frequently, this may create the situation where the authority of the panel and its report will be undermined. On the other hand, the frequency of appeals may also bring up another issue, namely the handling capacity of the Appellate Body consisting of seven members on a part-time basis. One possibility of remedying this problem would be to increase the number of members.¹⁴⁵

In addition, the Appellate Body must refer to every single issues raised¹⁴⁶ in accordance with the "scope of appeal"¹⁴⁷ during the appellate proceeding. One, therefore, could envisage the Appellate Body being required to deal with a considerable amount of work within the limited period of time.¹⁴⁸ Thus the WTO, soon or later, may have to consider increasing the number of Appellate Body members and also to provide the members with full-time status, if a number of cases are appealed at the same time in the near future.

Furthermore, the duties given to the members of Appellate Body may cause certain problems. According to a member of the Appellate Body,¹⁴⁹ so far, they normally convene and spend sometime in Geneva almost once every month. Thus, if a member has a full-time position in his home country, this situation creates timetable and scheduling difficulties.

The last point to be covered here is that since the DSU stipulated an obligation on the Appellate Body to answer all the issues raised by the parties, the Appellate Body may have to face even controversial issues which could possibly be avoided under the

¹⁴⁴ The information was also from the interview with a member of the Appellate Body (May 1997, Geneva).

¹⁴⁵ In my view, for instance, adding two more members, which makes 9 members in total. This number enables for the Appellate Body to handle three cases at the same time without having the situation that any of the members sits in two cases.

¹⁴⁶ *Ibid.*, *supra* note 20, Article 17, para. 12.

¹⁴⁷ *Ibid.*, para. 6 of the DSU states that "...shall be limited to issues of law covered in the panel report and legal interpretations developed by the panel".

¹⁴⁸ *Ibid.* Article 17, para. 5. states 90 days as a maximum limit of time.

¹⁴⁹ The interview was conducted, during my internship at WTO (May 1997, Geneva).

practice of the old system of GATT, because it normally dealt only with one legal ground and mentioned the rest of issues raised only briefly. Nonetheless, this customary practice furthermore created unpersuasive panel decisions in some cases during the time of GATT.

(iv) Retaliation Measures

Retaliation measures (i.e. the suspension of concessions or other obligations) shall be authorised by the DSB through the new "negative consensus" requirement. It, therefore, would be quite feasible for a country which is willing to obtain authorisation for retaliation in comply with the rule.

A disagreement on the scale of retaliation is to be resolved by an arbitration procedure:¹⁵⁰ there would be a sort of "check-and-balance" mechanism available to supervise the approved retaliation. In addition, under the new system, "cross-retaliation" is available to the complaining party in the case of suspension of obligations.¹⁵¹ Moreover, the necessity and degree of the cross-retaliation will also be determined through arbitration.¹⁵² Cross-retaliation thus will be regulated as to its effectiveness against retaliation measures.

(v) Implementation of the DSB's Decision

There will be a problem in implementing recommendations or rulings of the DSB. As stipulated in the DSU, the DSB shall keep under surveillance the implementation of any adopted recommendations or rulings, and any outstanding case will remain on the DSB agenda until the issue is resolved.¹⁵³ This presumably aims at imposing strong and persistent political pressure on the Member concerned. The Member concerned will be politically embarrassed since it made a commitment in public to agree with the WTO rules.

¹⁵⁰ *Ibid.*, Article 22, para. 6, *supra* note 97.

¹⁵¹ *Ibid.*, para. 3.

¹⁵² *Ibid.*, *supra* note 97.

¹⁵³ *Ibid.*, Article 21, para. 6, *supra* note 124.

Nonetheless, an issue of enforcement of the panel decision still remains unsolved. This issue also leads us to the question whether the suspension of concessions is an effective remedy. In this regard, for instance, we could possibly find an effective remedy in the following cases, in which "big economy (for example, the Quad members) wins against big economy", "big economy wins against small economy" or "small economy wins against small economy" cases were involved. In short, a remedy could be effective if there is great or fairly-balanced trade between the Member states concerned. However, there will not be an effective remedy in a case in which a small economy wins against a big economy because there is only a little volume of trade (i.e. unbalanced trade) between them. In that case, one could only expect a small scale of impact whoever wins, and therefore the impact of a remedy would be considerably limited.

Meantime, although the DSU provides a solution to the problem of blockage of panel reports to be adopted, and also provides a framework to initiate discussion on implementation, the real problem of the enforcement of the WTO rules will substantially depend on the individual economic influence or impact of the parties to the disputes. One may refer to the retaliation case under GATT cited earlier, i.e. the 1952 Netherlands retaliation case against the U. S. as a good example. Although the GATT contracting parties authorised the Netherlands to retaliate against the U. S. (i.e., an imposition of a limit of 60,000 tons on wheat flour imported from the U. S.) for failure to bring its practices into conformity with GATT obligations,¹⁵⁴ the Netherlands finally declined to exercise this authority. The reason for this lay in the secondary effects which would have appeared in the Netherlands. In other words, that action would have seriously affected the Dutch in general by causing higher prices for essential products such as bread. In short, the case demonstrated that "*generally everyone loses when a nation takes retaliatory action*".¹⁵⁵

¹⁵⁴ See, Hudec, R. H., *The Enforcing*, *supra* note 6, pp. 425-26.

¹⁵⁵ Bello, Judith H. and Alan F. Holmer, "U. S. Trade Law and Policy Series No. 24: Dispute Resolution in the New World Trade Organisation: Concerns and Net Benefits", 28 Int'l Law No. 4 (1994) at 1103.

Even under the new WTO system, this type of problem, i.e., "fairness of the rules and those systems *per se*" has not been removed. Perhaps, this could be considered as an issue relating to the nature of GATT/WTO system itself. In practice, a disadvantageous position of developing or least-developed countries is often the case in such rules and systems even though various provisions grant special favours to those members scattered over the whole system. After all, although WTO was set up to solve a great number of problems and ambiguities inherited from the old GATT system, perhaps the main goal of fair trade under the GATT/WTO system has not yet been achieved, particularly when it comes to questions at enforcements and remedies.

(vi) The issuance of the descriptive part of the panel report

The panel is required to issue the descriptive part, consisting of fact and argument, of the report in draft to the parties in dispute under Article 15: 1 of the DSU. However, one may wonder whether the issuance of this part is a necessary phase in the new dispute settlement procedure. From a historical point of view, the practice of the descriptive section prepared by the panel was essential in the old dispute settlement procedure of GATT where no other opportunity, such as the interim review in the WTO procedure, was provided for the parties to check the panel report in draft. The interim review of WTO offers the parties to the dispute an opportunity to check if the panel understands the arguments delivered by the parties properly, in advance of the issue of the final panel report. In addition, the disputing parties can predict, at this stage, the future decision of the case to be made by the panel via the interim report. The interim review stage therefore would be able to substitute for the issuance of the descriptive part of the report. Moreover, in fact, the time spent on the descriptive part of the review process is becoming short.¹⁵⁶ This could be explained because the review of the descriptive part is becoming a less confrontational process for the parties to the dispute. Thus one may argue that the panel process may be able to save

¹⁵⁶The paper by Davey, William J., "Issues of Dispute Settlement in the WTO System" at pp. 59-60, which was prepared for the forum "The Emerging WTO System and Perspective from East Asia" in 1996.

time at this stage and for such time to be used in another stage of the dispute settlement procedure without changing the present time limit.

(vii) Interim Review Stage

As briefly mentioned above, the interim review (Article 15 of the DSU) is one of the new features of the WTO dispute settlement procedure. This article states that the panel is required to issue an interim report (including the panel's findings and conclusions) plus descriptive sections (fact and argument of parties) to the disputing parties before the final report is circulated to the Members of the WTO. The main purpose of an interim review is: to avoid any obvious factual mistake in the draft for the final panel report; and to force the parties to reach a settlement. In addition, this stage can be regarded as an additional safeguard against mis-judgement, aside from the main safeguards provided by the Appellate Body. According to this provision, if there are no comments on the report from the parties within the suggested time limit,¹⁵⁷ the report will automatically become the final report. One may argue that there might be potential danger at this phase, that is, if the parties take advantage of this phase as a pre-appeal before reaching to the real appeal as provided in Article 17 of the DSU, in spite of the original objective of this instrument. The panel should maintain proper control over the parties not to do so.

5.5. Perspective of the New Dispute Settlement Mechanism

First of all, it is important to note that one of the central provisions of the DSU, Article 23, states that Members shall not make determinations of violations or suspended concessions, except through recourse to the dispute settlement rules and procedures of the DSU. This provision would certainly assist in preventing recourse to national rules for retaliation such as Section 301 of the Trade Act of 1974 of U. S., though, it may still be used in some situations¹⁵⁸ by private firms or industries to

¹⁵⁷The time period of the interim review stage must be within the duration defined in para. 8 Article 12 of the DSU (6 months as a general rule and 3 months in case of urgency).

impel the U.S. Trade Representative (hereinafter, the "USTR") to take unilateral action against an 'unfair trade practice'.

Whereas, the DSU makes it much easier to secure an approval, member states would therefore find it much easier to invoke the legalised retaliatory measures under the new WTO system. Namely, under the new rules, the Members would rely on the WTO, in the event of a losing party not following the panel decision, by obtaining an approval of their retaliatory action from the WTO.¹⁵⁹ In this respect, one may argue that the new system, in eliminating many opportunities for the respondent to delay the proceedings, will be favoured by complainants (the "complainants-friendly" system).

On the other hand, the new mechanism benefits those members who have been threatened or suffered damage by unilateral retaliation taken beyond the scope of the GATT/WTO dispute settlement procedures, because there is now an effective means standing up with unilateralism by bringing complaints against unilateral actions to the WTO.¹⁶⁰ However, the WTO has not yet eliminated unilateral measures itself completely but has narrowed the possibility of its usage under the system.¹⁶¹

Nevertheless, the U. S. has resurrected the Super 301 of the Trade Act of 1988,¹⁶² and specified a priority list of foreign practices at the end of September 1994 to be

¹⁵⁸ Further explanation on the possible situations is mentioned under (i) Unilateral Measures in Section 5.4. of the present chapter.

¹⁵⁹ Under the GATT, only one retaliatory measures have been approved; see, for instance, the United States v the Netherlands (1952) in *BISD 1S/32 (1953)*; in this case, however, in reality, the retaliatory measures which were granted to the Netherlands exposed a defective point of the GATT system, namely, the Netherlands' market was seriously affected due to the suspension of imported raw material (i.e., wheat flour) from the United States. Eventually, the Netherlands' retaliatory measures imposed on the imported wheat flour from the U. S. reflected a high price of bread in domestic market of the Netherlands; cf. On 9 April 1999, the U.S., pursuant to DSU 22.7, request that the DSB authorise suspension of concessions to the EC equivalent to the level of nullification and impairment i.e. \$191.4 million. On 19 April 1999, the DSB authorised the U.S. to suspend concessions to the EC as requested.

¹⁶⁰ For a good example, Japan/US Automobile disputes. In this case, Japan claimed against the U.S. for its unilateral measures and brought the dispute to the WTO. In fact, the dispute was resolved bilaterally before reaching to a panel stage. The relevant documents to this dispute is identified under *WT/DS6/...*; see Article 23 of the DSU.

¹⁶¹ See potential cases described in Section 5.4. of this chapter.

¹⁶² See an article, *Financial Times*, "Not so Super 301 after all", 6 October 1994 at 4.

targeted for Super 301 investigation. This suggests that the U. S. is going to continue to have recourse to unilateral retaliations to defend its trade interests despite the fact that it could be in violation of the WTO Agreement. However, under the new system, it is to be expected that Members will speedily inform the DSB of the matter. The U.S. therefore will not be able to take unilateral action as freely as it used to during the period of the GATT system. But, as mentioned earlier, the WTO has not yet eliminated unilateral measures itself completely but has narrowed the possibility of its usage under the system.¹⁶³ Therefore, we still have a dispute which argues the legality of unilateral measures, particularly the U. S. Section 301, under the WTO system (e.g. the Banana case).

Second, even if a large number of trade issues are now covered by the new WTO Agreement, once a dispute arises, it will be mainly decided on the judgements made by the panellists. The WTO Agreement, therefore, requires that the panellists be experts of international trade law or public officials who have previously served in areas dealing with trade policy.¹⁶⁴ As mentioned earlier, given the importance of the panels themselves, special attention needs to be paid to the way in which panellists are chosen.¹⁶⁵ This is true, particularly as far as the Appellate Body members are concerned, because of their longer period of service in office (once appointed as a member who will serve at least for four years, and can be reappointed only once),¹⁶⁶ compared to ordinary panellists who will be appointed for each case (i.e. the period

¹⁶³ See potential cases described in Section 5.4. of this chapter.

¹⁶⁴ *Ibid.*, *supra* note 20, Article 8, para. 1.

¹⁶⁵ Normally, as soon as a panel is established, the panel secretary who is from the operational division of the WTO Secretariat, suggest a list of suitable candidates for nomination to the panel (as panellists) from the indicative list of governmental and non-governmental panellists to the disputing parties. In practice, however, it is rare that the parties agree with the candidates listed up first time, by the panel secretary. In an extreme case, the parties reached an agreement on members of the panel after receiving the secretary's suggestion several times (i.e., According to the WTO Secretariat, the time from the establishment of a panel to the composition of a panel is, in average, 5.5 weeks according to the WTO Secretariat data of 1997). Thus, it could be quite a time consuming phase of the dispute settlement procedures, though, have to be extremely careful in choosing panellists.

¹⁶⁶ *Ibid.*, *supra* note 20, Article 17.

would be a matter of year or so). In addition, the decision made by the Appellate Body shall be final, which therefore increases the importance of their decisions.

Lastly, the WTO members have made a commitment to use a multilateral approach to settle their disputes (Article 23 of the DSU). Nonetheless, the economic blocs, such as EC and NAFTA, are most likely to resolve disputes within their own systems as long as disputes arise between their members. On the other hand, the economic bloc might bring a claim to the new WTO system as regards any dispute involving countries which are also members of the WTO. In other words, economic bloc could differentiate between types of dispute, namely, those disputes to be taken to the WTO system (multilateral trading framework) on one hand, and those disputes to be settled under the legal system of the economic bloc on the other. In that sense, for the time being, the bloc would still maintain the possibility of "forum shopping" or "rule-shopping" (which provides the members of economic blocs with more than one court and also rule to choose between for resolving disputes, whichever rule brings more favourable results), which was criticised during the GATT period. Perhaps, the choice underlying such decisions will depend on the level of the political, social, and economic priority of each individual case. Given this, it may be concluded that there will be certain advantages for the members of certain economic blocs to resolve trade disputes under their own bloc rule: the new dispute settlement mechanism of the WTO will leave the matter to a member's discretion just as GATT did in the past.

PART TWO

JAPAN: ITS EXPERIENCE OF INTERNATIONAL TRADE DISPUTES UNDER THE GATT/WTO

Chapter 6. THE LEGAL SYSTEM OF JAPAN

Introduction

The main purpose of this chapter is to provide an overview of the legal system of Japan. The chapter also deals with the constitutional issues which arise as between the domestic laws of Japan and international agreements, in particular, the position of GATT/WTO under the Japanese legal system. The chapter therefore will provide us with a concise picture of Japan's legal structure and its understanding of GATT/WTO.

6.1. An Overview of the Japanese Legal System¹

6.1.1. A Legal History of Japan's Modernisation

In order to comprehend the present attitude towards international trade law in Japan, it is necessary to make a brief reference to Japanese legal history, and in particular its westernisation emerged at the end of the 19th century.

In a sense, setting the tone for the future, the turning point for modernisation in Japan occurred in 1868, the year in which the goal: "overtake the West" was expressed. It is known by historians as the Meiji Restoration (or "*Meiji Ishin*" in Japanese) and set the tone for the future. Until then, Japan was under a system close to what in the West is known as medieval feudalism. Indeed, the whole of the country was divided into small principalities or clans called "*Hans*", each one of them ruled by their own feudal lords. Among those "*Han*", the Tokugawa Clan, the largest of them all, dominated the country and exercised control over the rest of the

¹See Matsushita, Mitsuo., International Trade and Competition Law in Japan, [hereinafter, the "Int'l Trade and Competition Law], Oxford University Press, Oxford, 1993.

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clans for over 250 years.² A historical event took place in 1853, when the American fleet, the "Black Ships" under Commodore Matthew Calbraith Perry, called at one of the Japanese ports, the port of "Uraga". Perry presented a letter from President Fillmore to the Tokugawa Government ("*the Bakufu*"), addressed to the Japanese Emperor. The letter was a petition from the United States demanding that Japan open up for trade with the rest of the world. Japan took the request made by Western countries as a threat, but, in any event, the Tokugawa Government finally decided to re-establish relations with the world.³ In 1858, Japan concluded commercial treaties with the United States.⁴ It was followed by similar agreements with England, France, Russia and the Netherlands. The treaties which Japan accepted, however, contained unfavourable conditions for the country. This situation is unsurprising, as it clearly reflects the Japanese history of the period, known in history as the period of "national isolation", the imposition of unfavourable conditions being compounded by Japan's inexperience of the rules and practice of international law in general.

Accordingly, these events had a profound impact on the country. Nationalistic sentiment grew among the ruling class ("*Samurai*") specially as the international situation had brought Western countries together, and it was perceived in Japan that it was urgent for the country to be unified under one Emperor so as to deal more effectively with attempts of domination by foreign powers. As a result of this, the alliance, composed of southern clans such as the "*Satsuma*" and "*Choshu*", succeeded in bringing about the collapse of the rule of the Tokugawa Clan and with its demise, the feudal system was abolished and replaced by a new regime. Under the restoration programme, new organs were created, i.e. a central government and prefectures (administrative subdivisions of the country) and the Emperor became a centre for the unity of the nation as a divine appointee. This unified "modern" state was thus established and Japan entered the 20th century.

²For description of this period, see Sansom., George, A History of Japan (1615-1867), Vol. 3, Wm Dawson & Sons Ltd., Kent, rep. 1978 at pp. 228-242.

³The period of national isolation or exclusion policy (known as "*sakoku seisaku*" in Japanese) was introduced in 1625, which was an order to close Japan to foreign trade and travel with a few strictly limited exceptions came in at the early seventeenth century (e.g. the orders of 1633, 1635 and 1639 are described as the three Exclusion Decrees).

⁴The treaty is called "*Nichibei shuukou tsuushou jyoyaku*" (in Japanese).

6.1.2. A Glance at Modern Japanese Laws⁵

This rapid shift from one system to another is also reflected in the reforms made to the legal system of the country. The Japanese legal system is composed of codes and statutes, which were imported at different times from Europe and the United States. The backbone of this system is a collection of six basic codes ("*Roppou*" in Japanese): (1) the Constitution⁶; (2) the Civil Code⁷; (3) the Commercial Code⁸; (4) the Code of Civil Procedure⁹; (5) the Criminal Code¹⁰; and (6) the Code of Criminal Procedure¹¹. In addition to these six basic codes, there are several important areas of the law such as administrative law, tax law, labour and employment law, social security law, public international law, law on conflict of laws, i.e., international private law, and economic law which regulates such matters as Antidumping Law, a number of laws regulating foreign trade and investment, and laws governing industrial policy.¹² The basis for those bodies of written law was the law of

⁵See, in general, for Japan's legal system, Dean, Meryll., Japanese Legal System: Text and Materials [hereinafter, the "Japanese Legal System"], Cavendish Publishing Limited, London, 1997.

⁶The Constitution, enacted in 1946, defines the basic framework of the government by providing for the Emperor (Chapter I), the renunciation of war (Chapter II), the rights and duties of the people (Chapter III), the Diet (Chapter IV), the Cabinet (Chapter V), the Judiciary (Chapter VI), the Finance (Chapter VII), the local self-government (Chapter VIII), the amendments (Chapter IX), the supreme law (Chapter X), the supplementary provisions (Chapter XI). Pursuant to the Constitution, the basic organs of the state are the Diet, "*Kokkai*" (the legislature), the Cabinet, "*Naikaku*" (the administration or executive), and the Judiciary, "*Saibansho*" (the Supreme Court and lower courts).

⁷The Civil Code, enacted in 1896, was modelled on the French Napoleonic Code and later influenced by the German Civil Code. The Code defines the basic law for private rights and relationship between private entities. The Code consists of five books: the general part, real rights, obligations, family law, and succession.

⁸The Commercial Code was enacted in 1899. The Code, however, has been amended many times due to the necessity of Japan, as a country which decided to modernise only a century ago based on the model of the Western countries, to catch up with the economic and social changes. Although the Code was modelled after German commercial law system, the present Commercial Code is a mixture of German, American, and traditional Japanese rules. Moreover, the Code is supplemented by a number of special laws like the Law on Bills and Notes and the Law on Limited Liability Companies.

⁹The Civil Procedure Code, enacted in 1890, was based almost entirely on the German civil procedure law. The Code defines rules for civil litigation and related matters such as jurisdiction of the courts, parties, oral arguments, evidence, and appeals.

¹⁰The Criminal Code, enacted in 1908, defines the general rules governing crime and punishment like the interpretation of crime, self-defence, emergency, and various forms of crimes and the punishment.

¹¹The Criminal Procedure Code, originally enacted in 1891, was modified after the Second World War. The Code provides for the provisions governing the trial of crimes under the Criminal Code and also supplementary laws.

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continental Europe. Under the Meiji Restoration, the Japanese codes were primarily modelled on German and French examples. Although the main purpose of this chapter is not to analyse the Japanese legal system, it is however useful to have a general view of the major areas of the law in Japan in order to understand the relationship between GATT/WTO and the relevant domestic law of Japan.

6.1.3. The Structure of the Japanese Government

In a study such as this, reference to Japanese Public Law is essential. According to Article 41 of the Constitution of Japan (hereinafter, the "Constitution"), the National Diet is the highest and the sole legislative organ of the state. The Cabinet is the executive organ (Article 65 of the Constitution). The Supreme Court and lower courts are the judicial organ (Article 76 of the Constitution). These three branches are separate. According to Article 98 of the Constitution, the Constitution is the supreme law of the nation, therefore none of the legislative, executive or judicial branches may violate its provisions. In the following sections, further details of each will be given.

6.1.3.1 The Legislative Branch (Chapter IV. of the Constitution: The Diet)

Article 41 of the Constitution states that the Diet is the highest organ of state power, and is the sole law-making organ of the State. The National Diet is composed of two Houses, namely the House of Representatives (the lower house or "*Shuugiin*" in Japanese) and the House of Councillors (the upper house or "*Sangiin*" in Japanese) (Article 42). Although a bill can be introduced either by members of both houses or by the Cabinet, in fact, in line with the situation in many other liberal democracies, the majority of bills that are passed and become law are introduced by the Cabinet.¹³

¹²See generally, Noda, Yoshiyuki., Introduction to Japanese Law , University of Tokyo Press, Tokyo, 1976; for further descriptions on the six basic codes of Japan, see *ibid.* at pp. 187-215.

¹³"From 1947 to 1983, out of 6,225 bills submitted to the Diet, 67% of them were submitted by the Cabinet while the rest were submitted by the members of the Diet. Of the bills actually passed by the Diet, 85 % were submitted by the Cabinet." (these data are from Oda,

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Nonetheless, there is no explicit provision in the Constitution which empowers the Cabinet to submit a bill but there are legal provisions concerning the Cabinet. A bill becomes law after a majority vote in both houses is taken and an approval of both houses is obtained; in the event that a bill which is passed by the House of Representatives, and upon which the House of Councillors makes a decision different from that of the House of Representatives becomes law when passed a second time the House of Representatives by a majority of two-thirds or more of the members present. The provision of the preceding paragraph does not preclude the House of Representatives from calling for the meeting of a joint committee of both Houses; if the House of Councillors fails to take final action within 60 days after the receipt of a bill passed by the House of Representatives - time in recess excepted - the House of Representatives may decide to reject the bill introduced by the House of Councillors (Article 59). Concerning a budgetary matter, the recognition of the supremacy of the House of Representatives is clear (Article 60). In addition to budgetary matters, this supremacy mentioned above applies also to the approval of the Diet for the conclusion of treaties (Article 61).

One point concerning the legislative procedure should be mentioned.¹⁴ Although a legislative bill can be introduced into the National Diet either by members of either of the two Houses or by the Cabinet, bills passed by both houses are, in most cases, prepared by Ministries in charge of the particular matters addressed in the bill and introduced by the Cabinet.¹⁵ For example, trade policies are formulated and implemented through close co-operation between the Cabinet and the National Diet, and also as is common with other democracies, the ruling political party or parties have considerable say. Moreover, conflicts between the legislative branch (the National Diet) and the executive branch (the Cabinet) over the policies are rare because of the parliamentary cabinet system.¹⁶ Although the principle of "separation

Hiroshi., Japanese Law, Butterworths, London, 1992 at 46).

¹⁴For further details on the legislative procedure in Japan, see, *ibid.*, pp. 46-49; cf. For comparison to the legislation procedure of the United Kingdom, see Loveland, Ian., Constitutional Law, Butterworths, London, 1996 at pp. 152.

¹⁵For further description on this matter, Matsushita, M., Int'l Trade and Competition Law, *supra* note 1 at 5-6.

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of powers" exists in Japanese constitutional law, the executive could be a part of the legislative power. In other words, it seems that there is already a high degree of consensus achieved through negotiation and compromise to obtain approval of a bill when the bill is at the preparation stage. On the other hand, the executive branch maintains a high degree of discretionary power, on its own, in formulating and implementing trade policies of the Japanese government due to the supremacy of the Cabinet.

6.1.3.2 The Executive Branch (Chapter V. of the Constitution: The Cabinet)

With respect to the structure of the executive branch, it is the National Government Organisation Law¹⁷ which defines its organisation. According to this law, the executive branch consists of the Prime Minister's Office ("*Fu*"), the Ministry ("*Shou*"), the Commission ("*Iinkai*"), and the Agency ("*Chou*"). There is one Prime Minister's Office and twelve Ministries in the executive branch. Among those Ministries, one which is particularly relevant in this study is the Ministry of International Trade and Industry (MITI), which is responsible for the formulation of trade policies and co-ordination of their implementation, and holds the legal power to control exports and imports.¹⁸ For example, the MITI is responsible for promoting and supervising industrial policy, granting industrial property rights through the Patent Office, licensing and regulating public utilities through relevant laws, and enforcing foreign trade policy through the Foreign Exchange and Foreign Trade Control Law. All of these areas touch upon important matters which concern GATT/WTO.

According to Article 65 of the Constitution, the executive powers are vested in the Cabinet. The Cabinet comprises the Prime Minister as its head, and other Ministers

¹⁶Jackson, John H., William J. Davey and Alan O. Sykes Jr., International Economic Regulations, 3rd ed., West Publishing Co., St. Paul, Minn. 1995 at 217.

¹⁷*Kokka Gyosei Soshiki ho*, Law 120, 1947, see Matsushita, M., Int'l Trade and Competition Law, *supra note 1*, footnote 6 at 7.

¹⁸For the structure of Japanese trade policy formation, see The GATT Secretariat, Trade Policy Review - Japan 1992, Vol. I, GATT, Geneva, January 1993, 33 *et seq.*

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of State; all of the Cabinet members must be civilians; and in exercising executive power, the Cabinet must be collectively accountable to the National Diet (Article 66). The Prime Minister is designated from among the members of the Diet by a resolution of the Diet although, in practice, the head of the ruling political party in the National Diet is nominated as the Prime Minister (Article 67). The Prime Minister, representing the Cabinet, submits bills, reports to the National Diet important matters concerning domestic affairs and international relations and supervises the various administrative agencies (Article 72). In addition to general administrative functions, the Cabinet is also responsible for carrying out the following functions: to administer the law faithfully and perform affairs of state; to manage foreign affairs; to conclude treaties (for that, it is necessary to obtain a prior consent from the National Diet but if the Cabinet fails to do so, a subsequent consent from the National Diet is required.)¹⁹; to manage the civil service in accordance with standards established by law; to prepare the budget and submit it to the National Diet; to enact cabinet orders to execute the provisions of the Constitution and laws; and so on (Article 73). All laws and cabinet decrees must be signed by the relevant Ministers and countersigned by the Prime Minister (Article 74).

6.1.3.3 The Judicial Branch (Chapter VI. of the Constitution: Judiciary)²⁰

Japan has had a unitary court system since 1947, therefore, the whole judicial system including civil, criminal, and administrative matters comprises a single hierarchy of courts. All courts are called "*saibansho*" in Japanese. In Japan, two classes of courts, i.e., the Supreme Court and the subordinate or lower courts, are distinguished according to the Law on Courts of 16 April 1947.²¹ According to Article 76 of the Constitution, the whole judicial power is vested in the Supreme Court and lower courts as established by law; the judiciary is independent from the other branches of

¹⁹This particular function of the Cabinet will be dealt with later in Section 6.2. (The Status of International Trade Agreements in Japan) of this chapter.

²⁰See generally, Noda, Y., *Introduction to Japanese Law*, *supra* note 12, pp. 119-138; also see, *Japanese Legal System*, *supra* note 5, pp. 391-401 and 405-417.

²¹In accordance with Article 76 of the Constitution of Japan.

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government, all judges must exercise their powers independently and are bound only to the Constitution and laws. The Supreme Court is authorised to enact rules concerning the procedure and practice of trials, the discipline of lawyers, the internal discipline of the courts, and the administration of judicial affairs; Public prosecutors are subject to the rules imposed by the Supreme Court. The Supreme Court may delegate the power to establish rules for lower courts to those courts (Article 77). Article 78 of the Constitution guarantees the security of the judiciary. The Supreme Court consists of a Chief Justice and other justices whose number is determined by law; the justices of the Supreme Court, with the exception of the Chief Justice, are appointed by the Cabinet (Article 79). According to Article 6 of the Constitution, the Chief Justice of the Supreme Court is appointed by the Emperor on the advice of the Cabinet. The Supreme Court is the authority of last resort in determining the constitutionality of any law, order, regulation or official act (Article 81).

The Supreme Court ("*Saikou saibansho*"), located in Tokyo (Article 6 of the Law on Courts), gives judgement only on questions of law. The Supreme Court is obliged to accept the findings of fact of the lower court against whose decision an appeal has been filed. According to Article 9 of the Law on Courts, the Supreme Court sits either as a full court (i.e. Grand Bench or "*Daihoutei*" in Japanese) or in divisions depending on the importance of the case in question; the full court consists of all the 15 justices along with the presiding Chief Justice; a quorum, the minimum number which is necessary to make a formal decision, is nine justices. A division (i.e. Petty Bench or "*Shohoutei*" in Japanese) is composed of at least five justices; a quorum being three.

The second level of jurisdiction comprises eight superior courts, called 'high courts' ("*Koutou saibansho*") and they are located in places such as Tokyo, Osaka, Nagoya, Hiroshima, Fukuoka, Sendai, Sapporo, and Takamatsu. There are divisions in each high court and each one has three or five judges. Appeal cases from the decision of district courts are dealt with by the high court.

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The district court ("*Chihou saibansho*") is the court of first instance under the current judicial system. District courts are located in each prefecture (though, four in Hokkaido), accordingly their total number is 50. A district court hears both civil and criminal cases except certain cases heard at first instance by the superior courts or by summary courts ("*Kani saibansho*")²². The Supreme Court appoints the judges and assistant judges of the district court, which is usually composed of one judge except in important cases, which require a bench of three judges.

6.2. The Status of International Trade Agreements in Japan

In this section the status of international trade agreements in the context of the Japanese legal system will be discussed. Among international trade agreements, those to which Japan is a party, especially the General Agreement on Tariffs and Trade (GATT 1947) and the WTO Agreement,²³ will be examined here.

There are a number of different forms of international agreements in which the Japanese government may be involved as a party. In Japanese legal terminology, those agreements are, for example, treaty ("*jouyaku*"); convention ("*kyouyaku*"); agreement ("*kyoutei*"); arrangement ("*torikime*"); declaration ("*sengen*"); protocol ("*giteisho*"); act ("*ketteisho*"); exchange of notes ("*koukanbunsho*"), and memorandum ("*oboegaki*").²⁴ According to the Constitution of Japan, "treaties" are regarded as the most formal style of international agreements. If the Japanese

²²The "summary" courts ("*Kani saibansho*") are placed at the lowest hierarchical level in the whole judicial system. Their decisions can be taken on appeal to the district court. The summary courts have jurisdiction in matters of which the value does not exceed 900,000 yen and criminal cases of minor offences. There are 448 summary courts and each of them is composed of one or more judges who are normally lawyers but lay persons may be appointed as well because a special knowledge of law is not essential to be the judge of a summary court. In the summary courts, cases are heard by only one judge, and of course, there are no divisions. The procedure of the summary court is quick and simple in order to make justice more accessible.

Although it is not important for the main focus in my thesis, there is another kind of court on the same hierarchical level as district courts, known as the family courts ("*Katei saibansho*"). Their jurisdiction is limited to cases of domestic matters and juvenile delinquency. The number of family courts is 50, which is the same as district courts and it is composed of a number of judges and assistant judges as appointed by the Supreme Court.

²³See Saito, Aki., "The WTO Agreement and the Relevant Japanese Domestic Laws", 30 J.W.T., No. 3 (June 1996), pp. 87-108.

²⁴See Matsushita, M., *Int'l Trade and Competition Law*, *supra* note 1 at 28.

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government signs an international treaty which *shall be faithfully observed* as stated in Article 98(2) of the Constitution, it implies that treaties prevail over any other law in Japan.

With respect to the process of approval of treaties in Japan, Article 73(3) of the Constitution states that the Cabinet has the authority to conclude treaties with foreign nations. The Cabinet, however, must obtain prior or, depending on the circumstances, subsequent approval by the National Diet. The procedure of approval of treaties by the National Diet, according to Article 61 of the Constitution of Japan, requires that the House of Representatives makes a decision first, and, according to Article 60(2) of the Constitution in the event of disagreement with the House of Councillors, then the decision of the House of Representatives shall prevail.

Since the War, there have been a number of times where the Cabinet has sought subsequent approval of the National Diet in exceptional circumstances.²⁵ The Protocol of Terms of Accession of Japan to the GATT, by which Japan acceded to the GATT,²⁶ is one of those exceptional cases: five cases out of eleven exceptional cases related to the General Agreement.²⁷

²⁵There are eleven cases (this data is from Orita, Masaki., "Practices in Japan Concerning the Conclusion of Treaties," [hereinafter, the "Practices in Japan"], 27 Japan. Ann. Int'l L. (1984) at 61 in footnote 19).

²⁶The National Diet approved the Protocol on 29 July 1955 subsequent to the signature of the Japanese government on 7 June 1955. There were two conditions to be met in order to make the Protocol effective: first, the signature of Japan, which met on 7 June 1955; second, according to Article 10 of the Protocol, a decision of two-thirds of the Contracting Parties' approval for Japan's accession, which met on 11 August 1955.

²⁷Those five cases are: (1) Declaration Regulating the Commercial Relations between Certain Contracting Parties to the General Agreement on Tariffs and Trade and Japan (obtained a subsequent approval from the National Diet in 1953); (2) Process-verbal Extending the Validity of the Declaration of 24 October 1953 Regulating the Commercial Relations between Certain Contracting Parties to the General Agreement on Tariffs and Trade and Japan (obtained a subsequent approval from the National Diet in 1953); (3) Protocol of Terms of Accession of Japan to the General Agreement on Tariffs and Trade (obtained a subsequent approval from the National Diet in 1955); (4) Document Relating to the Results of Negotiations with the Government of the United States of America for the Modification or Withdrawal of Concessions in the Schedule XXXVIII/ Japan (obtained a subsequent approval from the National Diet in 1961); (5) Document Relating to the Results of Negotiations with the Government of the Federal Republic of Germany for the Modification or Withdrawal of Concessions in the Schedule XXXVIII/ Japan (obtained a subsequent approval from the National Diet in 1961).

Concerning the WTO Agreement, the Diet's approval was obtained before Japan's ratification of that agreement. On 5 April 1994, the government of Japan signed the Final Agreement of the Uruguay Round at a Meeting in Marrakesh, Morocco held on 15 April 1994 in order to confirm its acceptance of the results of the round. On 1 December 1994, the lower house approved the agreement, then the upper house did so on 8 December. Thus, on 8 December 1994, the Japanese government obtained formal consent from the National Diet to ratify the agreement.²⁸ Finally, on 27 December 1994, the Government of Japan submitted an instrument for ratification of the agreement.

6.2.1. The Question of Validity of Treaties ("Treaties"/"Executive Agreements")²⁹

There is no distinction between "treaties" and "executive agreements" in international law, namely, both are considered to be treaties. In the domestic law of Japan, however, the Constitution makes a distinction between "treaties" and "executive agreements" which is somewhat confusing. First of all, the question of the validity of treaties in Japan has to be distinguished from the question of their direct applicability. The former question identifies whether treaties have the force of law in Japan and are part of Japanese law. Is there any difference between those two

²⁸See for Japanese translation of Marrakesh Agreement Establishing the World Trade Organisation, *Gaimusho* [Ministry of Foreign Affairs] (ed.), *Sekaihouekikikan wo setsuritsusuru Marrakesh kyoutei - WTO, Kokusaimondai kenkyujo*, Tokyo, 7 July 1995, pp. 334-351; for promulgation of treaties in Japan, Article 7 of the Constitution stated that the Emperor, with the advice and approval of the Cabinet, shall perform promulgation of treaties in matters of state on behalf of the people. In short, once the Cabinet conclude treaties (nonetheless, it shall obtain prior, depending on circumstances, subsequent approval of the Diet), the treaty is promulgated in the Official Gazette ("*Kampou*" in Japanese) under the name of the Emperor and the Cabinet. By the act of promulgation ("*Koufu*" in Japanese), a treaty is incorporated into Japanese law, in other words, gains the force of law and becomes a part of law in Japan. Cf. Regarding executive agreements, they appear in the Official Gazette as notifications ("*Kokuji*" in Japanese) under the name of the Ministry of Foreign Affairs or any Ministry which is in charge of the agreement.

²⁹For overview concerning legal systems of member states, U.S.; E.C. (E.U.); Japan, and GATT are described in, Jackson, J.H., *Restructuring the GATT System*, Royal Institute of International Affairs, London, 1990 at pp. 30-35.

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types of agreement in their binding force? What is the impact of this domestic categorisation of international agreements on GATT/WTO?

It is the government which decides whether an international agreement is to be considered a "treaty" or an "executive agreement".³⁰ As explained, "treaties" require the approval of the National Diet, whereas "executive agreements" do not. Article 73(2) of the Constitution states that the government, under its authority to conduct foreign affairs, can conclude international agreements without the approval of the National Diet, and those international agreements are called "executive agreements". It is true that there is no definition regarding the meaning of the term "treaties" in the Constitution. Unsurprisingly, therefore, the National Diet has often challenged the government on the issue of distinction between "treaties" and "executive agreements". In 1974, for example, the government tried to distinguish between "treaties" and "executive agreements". There were defined three categories which required the National Diet's approval to be defined as a "treaty".³¹ These three categories are as follows:³²

Category 1: an international agreement which involves 'statutory matters';³³

Category 2: an international agreement which deals with 'financial matters';³⁴
and,

Category 3: an international agreement which seems to have 'political importance'.³⁵

The first category is based on the principle that the National Diet must be "the sole law-making organ of the State" as stipulated in Article 41 of the Constitution. This category, therefore, contains the following agreements:

³⁰'Executive Agreement' is also termed as 'Administrative Agreements'.

³¹The Japanese government view concerning this issue was expressed in a statement made by the Foreign Minister M. Ohira which can be found in House of Representatives, Foreign Affairs Comm., Feb. 20, 1974, 72nd Diet, 5 *Gaimu iinkai giroku* 2, 27 Japan. Ann. Int'l L. (1984) at 102; see also, Orita, M., "Practices in Japan", *supra* note 25 at pp. 57-60.

³²See Iwasawa, Yuji, "Implementation of International Trade Agreements in Japan" [hereinafter, the "Implementation of Int'l Agmts in Japan"] at 305-306 in Meinhard Hilf and Ernst-Ulrich Petersmann (eds.), National Constitutions and International Economic Law, Kluwer Law and Taxation Publishers, Deventer, 1993.

³³Examples of the first category, see Orita, M., "Practices in Japan", *supra* note 25, in footnote 12 at 58.

³⁴Examples of the second category can be found, *ibid.*, in footnote 13.

³⁵Examples of the third category, *ibid.*, in footnote 14.

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- (i) an international agreement which needs the enactment of new statutes;
- (ii) an international agreement which demands the maintenance of existing statutes; and,
- (iii) an international agreement which affects the sovereignty of the state and modifies the power of the legislature as well, for example, a transfer of territory.

On the other hand, other agreements do not require the approval of the National Diet and thus are recognised as "executive agreements" and can be concluded by the government itself.³⁶ These include:

- (1) an agreement concluded within the scope of a treaty already approved by the National Diet;³⁷
- (2) an agreement concluded within the scope of domestic laws and regulations;³⁸ and,
- (3) an agreement concluded within the scope of budgetary appropriations.³⁹

As discussed earlier, the Protocol of Terms of Accession of Japan to the GATT⁴⁰ is to be considered as a "treaty". Its approval was given subsequent to being signed by the government.⁴¹ According to an official of the Ministry of Foreign Affairs, the GATT needed an approval of the National Diet as a "treaty" because it was an international agreement requiring the maintenance of existing legislation as indicated above.⁴² In addition to the GATT, most of the Tokyo Round agreements were

³⁶See *ibid.*, at pp 59-60; also see Iwasawa, Y., "Implementation of Int'l Agmts in Japan", *supra* note 32 at 306;

³⁷For examples of such type of agreements, see Orita, M., "Practices in Japan", *supra* note 25, in footnote 16 at 60.

³⁸For examples of such type of agreements, see *ibid.*, in footnote 15.

³⁹For examples of such type of agreements, see *ibid.*, in footnote 17.

⁴⁰For Protocol of Terms of Accession of Japan to the General Agreement on Tariffs and Trade, see BISD 4S/1.

⁴¹Like other countries, Japan signed the Protocol *provisionally* (i.e. Protocol of Provisional Application "PPA"). This should be counted as an exceptional case because of the link between signature and effectuation of the Protocol, see *ibid.*, para 10(a) at 10 (as for the WTO Agreement, there is no such provision). Furthermore, in the case of multilateral agreements in Japan, the ratification process happens in the following order: to sign an agreement; to obtain the Diet's approval; to submit an instrument of ratification; to enter into force.

⁴²See Iwasawa, Y., "Implementation of Int'l Agmts in Japan", *supra* note 32 at 307.

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concluded as "treaties" with the approval of the National Diet. Among those agreements concluded as "treaties", there were the agreements on tariff reduction; subsidies; antidumping; import licensing; and customs valuation. Furthermore, there are also a number of bilateral agreements concluded as "treaties" with the National Diet's approval.

With regard to "executive agreements" which require no approval by the National Diet, there are several multilateral trade agreements including some of the Tokyo Round agreements, for instance, agreements on dairy products and bovine meat which some makes this category. There are also bilateral agreements concluded as "executive agreements". For example, the Voluntary Restraints Agreements (hereinafter, the "VRAs"), including the 1972 Japan-U.S. Agreement on Textile Trade; the 1987 Japan-U.S. Agreement on Textile Trade; the 1986 Japan-U.S. Agreement on Steel Trade; the 1986 Japan -U.S. Agreement on Semiconductor Trade, and the 1987 Japan-U.S. Agreement on Machine Tools, were all concluded as "executive agreements" without the approval of the National Diet.

As can be observed, it seems that the distinction between "treaties" requiring the approval of the National Diet and "executive agreements" which do not require its approval is, in fact, necessary merely for the domestic procedures of Japan. In other words, the distinction between those two types of international agreement is maintained simply for Japan's constitutional purposes. Furthermore, in the Japanese legal system, there is no difference as regards binding force as between the two categories, namely "treaties" and "executive agreements". The government merely maintains the position that "treaties" are valid and thus have force of law in Japan as stated in Article 98 (2) of the Constitution. In addition, the courts also share the same view as the government.⁴³ Whereas, the "executive agreement", under the auspices of Article 98(2) of the Constitution, is a part of Japanese law once it is published in the Official Gazette.⁴⁴ Thus, it can be concluded that international

⁴³See, Iwasawa, Y., "Implementation of Int'l Agmts in Japan", *supra* note 32 at 311.

⁴⁴*Ibid.*, at 312.; there are commentators who deny the validity of executive agreements. For example, see Seki, M., "*Waga Kuni no Kokunai Ho toshiteno Jouyaku*" (in Japanese), 44

agreements, whether "treaties" or "executive agreements", are valid and have force of law in Japan once they are concluded properly and published in the Official Gazette.⁴⁵

6.2.2. The Question of Direct Applicability of Treaties

The question of the direct applicability of treaties in Japan should be distinguished from the question of the validity of treaties in Japan. The former question examines whether treaties are self-executing or not, i.e. whether they apply as law without the need for implementing legislation in Japan. Even though treaties have validity (force of law) in Japan, i.e. being part of Japanese law, this does not necessarily guarantee their direct applicability. Therefore, for example, if there is any conflict with domestic law, they might not apply directly in Japan. If they are not self-executing (directly applicable), in such a case, they need to be implemented by domestic legislation in order to be domestically applicable. According to Article 98(2) of the Constitution, it can be inferred that treaties are applicable as law in Japan. In fact, the Japanese courts have tended to accept that treaties were directly applicable once the courts confirmed their validity (force of law) in Japan under the auspices of Article 98(2).⁴⁶ Nonetheless, courts made some important judgements with regard to the question of direct applicability. The crucial issue in those judgements was "accuracy" of a treaty provision which was regarded as an essential criterion in determining its direct applicability. Bearing this point in mind, there is the *Shiomi* case to be examined here among other cases.⁴⁷

(No. 7) *Jichi Kenkyu* (1968) at 37, 46.

⁴⁵In the case of GATT, in 1955, the Japanese government promulgated the Protocol of Accession of Japan to the GATT and the schedules of concessions annexed to the Protocol in the Official Gazette. However, in fact, the GATT was finally published in 1966. Despite that, it is regarded that the GATT had acquired the force of law in 1955 through the due publication of the Protocol of Accession. It is noteworthy that a Japanese court recognised the validity of the GATT in 1961, in the *Kobe Jewellery* case (which will be dealt with later in this chapter), in advance of the formal publication of the GATT text in the Official Gazette. See, Iwasawa, Y., "Implementation of Int'l Agmts in Japan", *supra* note 32 at pp. 312-313.

⁴⁶*Ibid.*, at 315

⁴⁷See, *ibid.* at pp. 316-317.

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This case was concluded by the decision of the Supreme Court, which was handed down on 2 March 1989.⁴⁸ In the judgement, the court found Article 9 of the International Covenant on Economic, Social and Cultural Rights (hereinafter, the "ICESCR"), to which Japan was a party to be not directly applicable.

The petitioner was born in 1934 to Korean parents in Osaka. As Korea had been annexed to Japan since 1910, she was considered to be a Japanese citizen. In 1936, she became blind. In 1951, the time when Japan signed the Peace Treaty with the Allies and renounced all rights to Korea, she lost her Japanese nationality. Then, she was naturalised in 1970 after her marriage to a Japanese. After her naturalisation, she applied for a welfare pension under the Welfare Pension Law which came into force on 1 November 1959. However, her application was turned down in 1972 on the grounds that a pension could only be granted to a Japanese citizen and when this law came into effect she was not a Japanese citizen. She maintained that the rejection of her application for the pension was not in line with the ICESCR which stated in Article 9 "The State Parties [...] recognise the right of everyone to social security": this required the Japanese government to grant her pension rights.

Nonetheless, the Supreme Court rejected the petitioner's argument. The Supreme Court denied the direct applicability of Article 9 on the grounds that Article 2(1) of ICESCR states that the member states "take steps with a view to achieving progressively the full realisation of the rights recognised in the present Government [...]". According to this clause, it indicated that the Convention did not give a right on individuals but simply imposed an obligation on the member states gradually to take steps to realise the rights given in the Convention. As explained, there were clauses which explicitly stated the obligation of member states but the wording used in such clauses was unclear. In this case, it seemed that the "accuracy" of a treaty provision was considered as an important criterion in determining its direct applicability. To sum up, one may assume that if an international agreement is not drafted in sufficiently explicit wording, Japanese courts may rule that such an international agreement is not directly applicable and not self-executing.⁴⁹

⁴⁸Decision of the Supreme Court, 2 March 1989, 35 *Shomu Geppo*, (1989), 1754 *et seq.*

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Meanwhile, regarding the question of direct applicability of the "executive agreement", scholarly opinion is divided. One side states categorically that the "executive agreement" cannot be directly applicable. The other claims that the direct applicability of the "executive agreement" should not be denied due to categorical reasons.⁵⁰ In any case, it would be very difficult for the government of Japan to deal with the ever more demanding and increasing influences of foreign affairs in this modern society if the direct applicability of "executive agreements" were denied.⁵¹ In practice, the merits of an executive agreement is that the government can conclude an international agreement without the approval of the National Diet, which means an "executive agreement" is speedier and easier to conclude.

6. 3. The Application of International Trade Agreements

6.3.1. The GATT and the National Laws of Japan

In this section, we will focus on how the GATT was implemented into the Japanese legal system and also how effective it is vis-à-vis the national law of Japan. As discussed earlier, the General Agreement, including other international agreements such as the IMF Treaty and OECD, enjoy the status of a "treaty" in Japan pursuant to Article 98(2) of the Constitution. Nonetheless, in fact, there is no court decision as yet in the case as to whether a Japanese domestic law in conflict with an obligation of a treaty would be ruled invalid based on the provisions of Article 98(2). In this section, two major cases involving the GATT 1947 are analysed with respect to this issue.

First, the *Kobe Jewellery* case⁵² may illustrate the situation in point. A person had tried to smuggle jewellery into Japan with a declaration that the jewels were only

⁴⁹However, the factors for determining whether treaties are "directly applicable" in Japan can be found in the words used in it, the contracting parties' intention, and the circumstances in which treaties came into force. See, Matsushita, M., *Int'l Trade and Competition Law*, *supra* note 1 at 31.

⁵⁰Iwasawa, Y., "Implementation of Int'l Agmts in Japan", *supra* note 32, at 317.

⁵¹*Ibid.*

⁵²Judgement of the Kobe District Court, 30 May 1961, *Kakyu Saibansho Kiji Saiban Reishu* (Lower Court Criminal Cases Reporter), [hereinafter referred to as the "*Kakyu Keishu*"]

"personal belongings" when, in fact, they were for sale. The Kobe District Court therefore gave a ruling that the person was guilty of breach of the Customs Law. The defendant's argument, though rejected by the court, was based on Article VIII:3 of GATT, which stated that a contracting party shall not impose substantial penalties for minor breaches of customs regulations or procedural requirements. The defendant therefore argued that the Japanese government could not impose any penalty due to this provision. The District Court, however, held that the defendant was guilty on the grounds that his conduct was beyond the "minor offence" requirement stipulated in GATT Article VIII:3. The District Court referred to Article 98(2) of the Constitution and stated that "the principle of faithful observance of treaties [...] is understood to proclaim the superiority of treaties [over the domestic law of Japan]." Although the Court appeared to support the principle of the supremacy of treaties over the domestic laws of Japan, the judgement effectively overruled such principle in the end. The judgement was contradictory to the legal doctrine. Japanese law does not yet seem clear on this point, which is particularly relevant to the GATT position in domestic law.

Second, the decision in the *Kyoto Necktie* case, probably the most important decision concerning the relationship between treaties and domestic law in Japan,⁵³ is explored below. Three courts heard this case: the Kyoto District Court,⁵⁴ the Osaka High court,⁵⁵ and finally the Supreme Court.⁵⁶

3/5-6 (1961), 519 ff.

⁵³Two cases are noteworthy regarding the issue, those cases are: (1) the *COCOM Case of 1969*, and (2) the *Japan - US Textile Agreement Litigation of 1971*. The case (1) can be found in *Gyosai Reisyu* (Administrative Cases Reporter), Vol. 20, p. 842 (1969), and see for a comment on this case, Matsushita, M., "Export Control and Export Cartels in Japan", 20 *Harv. Int'l L. J.* (1979) at pp. 103 ff., 106-108; and also in Matsushita, M., *Int'l Trade and Competition Law*, *supra* note 1 at pp. 14-18. The case (2) has raised a legal issue, for the first time, with regard to the relationship between a government restriction of international trade and the GATT. In the end, the suit was withdrawn due to political reasons, and thus no court decision was handed down. In addition, the short explanation on those two cases also can be seen in Iwasawa, Y., "Implementation of Int'l Agmts in Japan", *supra* note 32 at pp. 318-320.

⁵⁴Judgement of the Kyoto District Court, 29 June 1984, 31 *Shomu Geppo* 207; also in 530 *Hanrei Taimuzu* (1984), 265 ff.

⁵⁵Judgement of the Osaka High Court, 25 November 1986, 634 *Hanrei Taimuzu* (1986), 186 ff.

⁵⁶Judgement of the Supreme Court, 2 February 1990, *Sosho Geppo*, 36/12 (1990), 242 ff.

The Decision of the Kyoto District Court:

With respect to the first decision, the Kyoto District Court dismissed the claim which was that the interests of the tie producers in the region of Kyoto (hereinafter, the "plaintiff") were adversely affected by restrictions on the imports and the high price of raw silk in 1984, and the court refused to apply the GATT as proposed by the plaintiff. In short, therefore, it denied the "direct-applicability" of the GATT rule at issue. The background to this case was quite complex, and thus further explanations are required.

Although Japan used to be the major exporter of raw silk, since the mid-70's its position had been overtaken by competitive neighbouring countries, especially Korea and the People's Republic of China. Japan, therefore, passed the Silk Price Stabilisation Law (hereinafter, the "Law") in an attempt to cope with the competition. In short, the Law guaranteed a minimum price for raw silk and created a government agency named the "Silk Business Agency" (or "*Sanshi Jigyodan*" in Japanese).⁵⁷ The government set regulated price limits for the product, both at the upper and lower ends of the scale. The system, under the Law and its regulation, functioned as follows: when the market price reached beyond the top limit, the Agency sold raw silk from its stockpile in order to lower the price and keep it within the price zone determined by the government [i.e. the Minister of Agriculture, Forestry, and Fisheries (hereinafter, the "MAFF")] in advance; whereas, if the market price dropped below the bottom limit, then the Agency would buy raw silk up to the price settled within the set price range. In theory, therefore, the price of raw silk could be maintained within the price zone targeted by the government. Ironically, however, this mechanism brought about overproduction of silk, with the correlative result of falling prices. The price stabilisation mechanism would have collapsed if lower-priced foreign raw silk had been imported without restrictions in the Agency's attempt to regulate the market. Moreover, even if the Agency had purchased all of the available domestic raw silk, the supply of the imported silk would have kept

⁵⁷When an amendment was made to the Silk Price Stabilisation Law in April 1981, the name of the agency was changed into "*Sanshisatorui Kakakuantei Jigyodan*". Under this new regime, no one was allowed to import raw silk from abroad, other than the government agency above mentioned and other consigned person or entity.

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pushing the domestic price down beyond the lower limit set by Law. Thus, it became imperative to amend the Silk Price Stabilisation Law to the effect that the Agency was vested with the exclusive right to import raw silk. The Agency would then sell the imported silk on the domestic market at a price within the price zone decided by the MAFF. As a result, this price stabilisation mechanism generated higher prices in the Japanese market than the international standard price. Indeed, the silk price soared in Japan to almost twice the world price.

Against this complex regulatory background, the necktie makers in the region of Kyoto (the plaintiff) had no alternative other than to use the over-priced raw materials of silk for their products. European necktie makers, however, could use inexpensive silk and then export their finished products to Japan. The European makers took full advantage of the import of cheap raw silk available (from Korea and the People's Republic of China). The Japanese government stepped in and imposed a 17 percent *ad valorem* tariff on imported ties in Japan. Nevertheless, domestic tie makers still could not compete with the Europeans.

Eventually, the necktie producers of Kyoto region brought a lawsuit in the Kyoto District Court against the Japanese government. The plaintiff claimed compensation for the losses caused by the price stabilisation programme. The plaintiff maintained that the government measure over-protected silk growers at the expense of tie makers, and that the government was unreasonable in restricting the right of tie makers to import silk freely, an action which in turn constituted violation of the "freedom of business" protected by Article 22(1) of the Constitution. The plaintiff further alleged that the government was in breach of Article II:4 and Article XVII of the General Agreement. Article II:4 prescribed that whenever a tariff concession under the GATT was made for a commodity for the purpose of state trading, a contracting party could not sell the commodity in the domestic market at a price higher than the real price plus tariff; while, Article XVII stipulated that state trading agencies were required to carry on their business merely in accordance with

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commercial considerations of price, quality, availability, marketability, transportation and other conditions under the general principles of non-discriminatory treatment prescribed in the GATT. The plaintiff argued that the Silk Business Agency was selling imported raw silk at a price determined artificially by the government, which established a breach of the GATT.

The Kyoto District Court held that the freedom of business activities assured under the stipulation of Article 22(1) of the Constitution was subject to the protection of public welfare and that, in addition, courts should avoid passing judgement regarding the wisdom of legislation intended to accomplish an aim of socio-economic policy.⁵⁸ The court, furthermore, held that domestic ties were protected by the tariff imposed on imported ties, that the government would be able to exercise rights under GATT Article XIX for taking safeguarding measures if the situation of local tie makers deteriorated seriously, and that therefore the plaintiffs had not been disproportionately disadvantaged by the governmental measures of protection of silk growers.

There are a few more issues worthy of consideration concerning this case. First, with respect to the compatibility with the GATT rules of the exclusive import system provided for by the Law, the court rejected the plaintiff's argument and then supported the validity of the Law and the measures taken for its implementation. The court stated that the exclusive import right and the price stabilisation mechanism were, in this case, designed to protect raw silk producers from the pressure of imports "for some time". Apparently, the idea was to give the measure the same effects as the "emergency measures" accepted under Article XIX.

The court also stated that the period for the exclusive right to import silk should be decided flexibly on a case by case basis, though, there should be a time limit taking into consideration that an "emergency measure" under the GATT rules is for a short

⁵⁸According to Professor Iwasawa, "Japanese courts follow a 'double standard' in reviewing the constitutionality of statutes", which means as follows: if the case relates to infringement of spiritual liberties, for instance, a freedom of expression, a *strict* scrutiny standard is required; whereas, in the case of the infringement of economic liberties, *less rigorous* scrutiny is enough. (emphases added), see Iwasawa, Y., "Implementation of Int'l Agmts in Japan", *supra* note 32 at 321.

time. The court further found that the provisions of the Law relating to the right of exclusive import could not be regarded as "unreasonable". Limits to the period for the exercise of the right should be determined in relation to the duration of the pressure on imports. Accordingly, with regard to the issue of emergency measures, the court agreed that the exclusive import right was not incompatible with Article XIX of the GATT which would permit such a measure. In the end, it became unnecessary for the court to tackle the issue of the effectiveness of the Law and the exclusive right to import raw silk as a domestic law vis-à-vis the GATT.

Disappointingly, the court stated its stance in the form of *obiter dicta*, which carries therefore little precedential value. The court stated that, in cases of a violation of the GATT, the GATT system would put pressure on the authorities to correct the violation at issue, by way of example, by issuing a request for consultation and taking retaliatory measures put forward by other member countries. Therefore, the court added that the GATT would have no more legal effectiveness in the country other than that resulting from those indirect influences. The court explained that even if a domestic law was inconsistent with the GATT, the domestic law would not be nullified simply for that reason. The court therefore implied in its stance that the domestic law prevails over the GATT.⁵⁹

The Decision of the Osaka High Court:

Following the first claim to the District Court of Kyoto, the necktie makers took the case on appeal to the Osaka High Court, where it was dismissed on 25 November 1986⁶⁰. With respect to the issue involving Article 22(1) of the Constitution, i.e. whether the exclusive right to import was contrary to the freedom of business activities as guaranteed under the Constitution, the court said that it compatible on the basis of its reasoning on the doctrine contained in previous cases.⁶¹ The

⁵⁹With respect to the position of treaties in the legal system of Japan, i.e., the ranking between treaties and statute; treaties and the Constitution, see, *ibid.* at pp. 328-331.

⁶⁰*Ibid.*, at 336.

⁶¹For cases, see "*Kourishijyou jiken hanketsu*", *Keishu*, Vol. 26, no. 9 at 586; "*Yakujihou iken hanketsu*", *Minshu*, Vol. 29, no. 4 at 572; the doctrine followed in those case are as follows: The national control/regulation over the freedom of business activities by law can be categorised into two groups, i.e. (1) the Positive one (which is, for example, a market control based on the social and economic policies, in order to protect an infant or small-scale

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appellants, in this appeal, also argued another issue, i.e. the compatibility of the exclusive right to import with the GATT and the validity of this law. Answering those points, the court somewhat twisted the issue by stating that the appellants argued that the sale price of imported silk was inconsistent with Article II:4 and Article XVII of the GATT and that the Silk Business Agency determined the sale price on the basis of the standard price set by the MAFF. Thereby, the court dismissed the argument made by the appellants on the grounds that it referred to nothing else but the action of the Silk Price Agency as the basis for the illegality of the legislation. In short, the argument made by the appellants was lacking in relevance.

The Decision of the Supreme Court:

The necktie producers appealed against the judgement to the Supreme Court and argued that according to Article II:4 of the GATT, a state agency shall not sell imported products in the domestic market at a price higher than the actual import price plus tariff, because the agency would obtain extra benefit if the imported products at issue were subject to a tariff concession stipulated in the GATT. In addition, the petitioners argued that pursuant to GATT Article XVII:1, each Contracting Party was supposed to guarantee that its state trading agency functioned merely for commercial considerations. The exclusive right to import is established pursuant to Articles, 12.13.2 and 12.13.3, of the Silk Price Stabilisation Law. However, these provisions of the Law are in contravention to Articles II:4 and

industry.), and (2) the Negative one (which is, for instance, a control for the purpose of providing health/ security for the national citizen.

With respect to the group (2), examine whether the control is within a minimum extent through a strict judicial investigation. Regarding the group (1), in principle, the decision by the legislature shall be respected concerning a regulation at issue. In short, the legislature regard a control as constitutional in general unless (i) the control (legislation) exceeds the discretion of the legislature, or (ii) the way of enforcement of the control is considerably unreasonable.

As the Silk Price Stabilisation Law (the Law) whose main purpose is to protect the silk producers, thus it belongs to the group (1) control. Accordingly, the test for constitutionality with regard to the exclusive import rights of the products provided for in the Law, in principle, should be decided by the legislature instead of the judiciary. Therefore, the decisions made by the three different courts over the constitutionality for the exclusive import rights were "yes", in short, "valid" with one accord.

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XVII:1. Thus, the enactment of the provisions under the Law was allegedly unlawful under the GATT, and in their view the National Diet had approved provisions of law which infringe on the GATT. The petitioners did not make a constitutional challenge based on the fact that the actions of the Silk Business Agency were inconsistent with the GATT, but claimed damages allegedly caused by this unlawful legislation.

On 6 February 1990, the Supreme Court dismissed the arguments of the petitioners. This decision was very short, though, controversial. The Supreme Court upheld the decisions given by the lower courts. The reason for doing so lay in the constitutionality of the exclusive right of the Agency to import raw silk under the Stabilisation Law. The court cited previous decisions passed by the Supreme Court, and noted that by taking precedents into consideration, the question whether domestic silk producers should be protected or not was simply a matter of policy and discretion, and therefore beyond any interference by the judiciary. The Court also noted that the decision made by the National Diet to protect domestic silk producers through the policy of the price stabilisation programme and exclusive rights to import, could not be legally challenged in court except in cases, for example, where the law provided protection for one party at immoderate expense to other parties, to society, or where the manner of achieving the legislative objective was not reasonable.

Nevertheless, the petitioner maintained that the exclusive right to import under the price stabilisation programme contravened articles of the GATT, and therefore they were invalid. Whether this reason given by the petitioner could be considered logical or not depends on the position of international treaties in the domestic legal order. It seems that the petitioner's argument was based on the notion of "treaty supremacy theory", (which means that in case of conflict between treaties and domestic law, the former prevails) subject to the direct applicability of the GATT in the Japanese legal system.⁶² Nonetheless, the issue (a domestic law based on its

⁶²See in general, Iwasawa, Y., "Implementation of Int'l Agmts in Japan", *supra* note 32 at

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alleged incompatibility with an international treaty) was not introduced as a constitutional challenge. Although the opinion over the relationship between treaties and the Constitution is divided, that is, between the "treaty supremacy theory" and the "constitutional supremacy theory", treaties concluded by Japan must be faithfully observed as stated in Article 98(2), but the challenge was not introduced as such. In the end, the Supreme Court simply stated that the judgement of the original court could be approved in the light of the reasoning given by the court, and thus, there was no illegality involved in this case.⁶³

Remarks on the judgements:

As we have observed, it is quite obvious that the Osaka High Court was mistaken in its understanding of the legal issue of the case, which was the illegality of the exclusive import right of the products provided for by the Law (the Silk Price Stabilisation Law) under the GATT rules, and reached a decision on the somewhat imprecise basis of the separation between law and policy.

First of all, if the arguments given by the petitioners in the court were not clear enough, the Osaka High Court should have exercised its power to request further explanations concerning the arguments of the petitioners in order to interpret the issue correctly and precisely. Furthermore, the Osaka High Court did not refer to the question of whether the exclusive right to import and the price stabilisation programme violated Article II:4 and Article XVII:1 of the GATT; or whether the measures taken pursuant to those provisions of the GATT could be considered to be a safeguard measure as granted under Article XIX of the GATT. According to Article XIX, a safeguard measure shall apply "if, as a result of unforeseen developments, any product is being imported into the territory of that contracting party in such increased quantities and under such conditions as to cause or threaten serious injury to domestic producers in that territory of like or directly competitive

328 *et seq.*

⁶³Professor Matsushita explained the judgement by stating that the Supreme Court might had been influenced by an "invisible" political pressure. See the conference paper by Matsushita, M., "State Trading in Japan", which was presented at The World Trade Forum (Trade Liberalisation and Property Ownership: State-Trading in the 21st Century) held in Gerzensee, Switzerland, 12-13 September 1997.

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products". In this case, however, an increase in the importation of a product, i.e., raw silk, was likely to be anticipated due to its competitive price. In addition, it was not proved that serious damage had been caused to domestic producers, because of imports of raw silk. Moreover, regardless of the limits of extent and time, as a matter of fact, the exclusive right to import provided excessive protection to domestic producers of raw silk, and consequently it became a permanent means of controlling imports. As shown, the measures clearly did not fulfil the requirements obliged by Article XIX. For this reason, the exclusive imports system provided for by the Law is unjustifiable under Article XIX of the GATT.

Now, if we look at the case from the point of view taken by the Kyoto District Court, the effect of a violation of a provision of GATT merely carries effects in international law. A violating country will be invited for consultation pursuant to Article XXIII of the GATT or will be made the subject of retaliation, but there will be no further legal effect apart from this. The necktie makers, however, expressed the opinion that the issue of measures intended to ensure the effectiveness of treaty obedience were totally different from the issue of the validity of a domestic statute infringing the GATT. This point brings a controversial issue to the fore, that is, the question of the "direct applicability" and "validity of a treaty" in the Japanese legal system.⁶⁴ With respect to the decision of the Kyoto District Court, there are a few other issues which merit further consideration. These concern the domestic validity of the Silk Price Stabilisation Law and of the exclusive right to import raw silk from abroad.

Let us look at the views of some Japanese scholars on this point. Professor Taira, for example, is of the view that Articles II:4 and XVII:1(a) of the GATT lack direct applicability because these articles are merely addressed, in a literal sense, to nations instead of individuals, and accordingly he agrees with the treatment of international

⁶⁴For an extensive study on this issue, see Iwasawa, Yuji., *Jyoyaku no Kokunai Tekiyō Kanousei - Iwayuru "Self-Executing" na Jyoyaku ni kansuru Ichi Kousatsu*, (in Japanese) [Domestic Applicability of Treaties: What Are Self-Executing Treaties?], Yuhikaku, Tokyo, 1985.

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law in judgement of the Kyoto District Court.⁶⁵ Those articles are, therefore, beyond the reach of individuals to utilise in a claim before a domestic court. Taking the contrary view, Professor Shimizu argued that Article II:4 was sufficiently clear and precise to be directly applied in this case and therefore, he criticised the opinion of the Kyoto District Court.⁶⁶ In his view, individuals were perfectly entitled to claim the applicability of those articles in a municipal court. Professor Matsushita follows in the line of Professor Shimizu's arguments, but he also believes that the National Diet should legislate in line with the requirements of Article 98(2) of the Constitution⁶⁷ which states that "treaties concluded by Japan and established laws of nations shall be faithfully observed". In that sense, Article 98(2) of the Constitution contains a very specific provision for the "supremacy of treaties" over any conflicting domestic laws. Furthermore, as argued above, it is generally recognised that the National Diet is duty bound not to legislate in breach of treaties. Therefore, it follows necessarily that a domestic law which violates a treaty should be invalid.

In the meantime, with regard to the issue of the direct applicability of the GATT, one may have noticed that the Japanese courts made two conflicting patterns of judgement. On the one hand, the courts found that the substantive provisions of the GATT were directly applicable as in the *Kobe Jewellery* case. While, on the other hand, the courts denied the direct applicability of the GATT in the *Kyoto Necktie* case, by passing a judgement which could be considered ill-judged, ambiguous, and based on questionable reasoning.⁶⁸ It is therefore unsurprising that the *Kyoto Necktie* case was strongly criticised by scholarly writings.⁶⁹ Moreover, these two cases might

⁶⁵Taira, Satoru., "Waga kuni ni okeru GATTO no Houteki Chii: GATTO no Chokusetsu Tekiyo Kanousei wo Chushin to shite [Legal Status of the GATT in Japan: Its Direct Applicability]" (in Japanese), 39 *Kobe Shoka Daigaku Shodai Ronshu*, No. 4, (1988), p432, at pp. 383-7.

⁶⁶Shimizu, Akio., "GATTO Ruru ni yoru Eigyo no Jiyu oyobi Zaisanken Koshi no Jiyu Hosho: Nishijin Nekutai Soshō Dai Isshin Hanketsu wo megutte [The Guarantee of the Freedom of Business and the Free Exercise of Property Rights by GATT Rules: The District Court Decision in the Nishijin Necktie Litigation]" (in Japanese), in *Kokusai Keizai Masatsu to Waga Kuni no Sangyo Seisaku* [International Economic Friction and Japan's Industrial Policy], 1987, p. 37 at p 43.

⁶⁷Takano, Yuichi., *Kempo to Jyoyaku* [Constitutions and Treaties] (in Japanese), University of Tokyo Press, Tokyo, 1960 at 209.

⁶⁸Iwasawa, Y., "Implementation of Int'l Agmts in Japan", *supra* note 32 at 344.

be regarded as a reflection of the lack of concern of the Japanese courts towards the arguments supportive of a mutually beneficial relationship between treaties and the domestic laws of Japan. Accordingly, it seems that it is essential for the Japanese courts to clarify their legal interpretation of issues involving international trading matters which are looming large in this fast-changing global trade environment especially after the establishment of WTO which included new areas such as services and intellectual property rights. Furthermore, the relevance of effective methods for resolving trading conflicts continues to grow, and thus the Japanese legal system should prepare itself to cope with future cases involving international trade. In addition, perhaps one would agree with the suggestion made by Professor Matsushita in his article, that it is our pressing need to produce judges who are well acquainted with international trade matters and furthermore, this need should also be addressed by the legal education system in Japan.⁷⁰

6.3.2. The Impact of GATT/WTO Panel/AB Reports And the National Laws of Japan

Let us move on to another important point of this section. This point concerns the effect of the resolutions/decision of international organisation, more specifically, recommendations or rulings of the CPs/DSB in the GATT/WTO panel/AB reports on domestic laws in Japan. No provision explicitly defines the status of actions of international institutions as such. This question has not as yet been resolved and still needs to be clarified to enhance the credibility and consistency of the Japanese courts and their view on this matter. Nonetheless, one may find that the extent to which Japan has approached this question so far is unsatisfactory. How did/does Japan react to the adopted GATT/WTO panel/AB reports? In Japan, GATT panel reports have generally been considered as "non-binding" by Japanese scholars.⁷¹ Although

⁶⁹For scholarly writings with a critical view, for instance, see Matsushita, M., "*Nishijin Necktie Soshou Saikousaihanketsu*", *Jurist* (in Japanese), No. 956 (1990.6.1), pp. 76-80; Iwasawa, Y., "Implementation of Int'l Agmts in Japan", *supra* note 32.

⁷⁰Matsushita, M., "*Nishijin Necktie Soshou Saikousaihanketsu*", *ibid.* at 80.

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such scholarly opinions are not regarded as a source of law in Japan, the courts often accept them and they influence judgements.⁷²

According to Article XXIII:2 of GATT 1947, "The CONTRACTING PARTIES shall promptly investigate any matter so referred [...] and shall make appropriate recommendations to the contracting party [...], or giving a ruling on the matter, as appropriate." Furthermore, panel reports need to be authorised in order to acquire the authority (i.e. a "binding" nature) through their adoption by the CONTRACTING PARTIES.⁷³ In addition, the Contracting Parties make findings which are merely a declaration of existing rights and obligations under the binding treaty.⁷⁴ The power of the Contracting Parties, i.e., authorisation of interpretations of the GATT may be deduced from both Article XXV of the General Agreement and Article 31:3 of the Vienna Convention on the Law of Treaties. That is, according to Article XXV, "[...] giving effect to those provisions of this Agreement which involve joint action and, [...] facilitating the operation and furthering the objectives of this Agreement". In addition, Article 31:3(b) of the Vienna Convention refers to "any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation".

The status of panel reports was dealt with under the WTO in both the reports of the panel and of the Appellate Body, which demonstrated a difference of opinion. The Panel concluded that:

...panel reports adopted by the GATT CONTRACTING PARTIES and the WTO Dispute Settlement Body constitute subsequent practice⁷⁵ in a specific

⁷¹Iwasawa, Y., "Implementation of International Agmts in Japan", *supra* note 32 at 336.

⁷²Oda, H., *Japanese Law*, *supra* note 13 at pp. 63-64.

⁷³Now, it is replaced by the DSB under the new WTO system; European Economic Community - Restrictions on Imports of Dessert Apples, **BISD 36S/93**, para. 12.1.

⁷⁴Iwasawa, Y., "The Relationship Between International Law and National Law: Japanese Experiences", 64 *Brit. Y. B. Int'l. L.* (1993) at 386.

⁷⁵See the report of the Appellate Body, **WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R** (4 October 1996), Section E, where it cited Article 31(3)(b) of the Vienna Convention and stated that "any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation" is to be "taken into account together with the context" in interpreting the terms of the treaty. It continued that, in international law generally, the essence of subsequent practice in interpreting a treaty has been recognised

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case by virtue of the decision to adopt them. Article 1(b)(iv) of GATT 1994 provides institutional recognition that adopted panel reports constitute subsequent practice. Such reports are an integral part of GATT 1994, since they constitute "other decisions of the CONTRACTING PARTIES to GATT 1947"⁷⁶

The general view under GATT 1947 was that the conclusions and recommendations made in an adopted panel report bound the disputing parties in that particular case, but subsequent panels were not legally bound by the details and reasoning of previous panel reports.⁷⁷ The Appellate Body of WTO stated in its report that the CONTRACTING PARTIES, in deciding to adopt a panel report, did not intend that their decision would constitute a definitive interpretation of the relevant provisions of GATT 1947 (neither in GATT 1994).⁷⁸ Furthermore, Article IX:2 of the WTO Agreement provides that the Ministerial Conference and the General Council shall have the exclusive authority to adopt interpretations of the Agreement and of the MTAs.⁷⁹ The WTO Agreement also defines the continuing relevance of the legal history and experience under the GATT 1947 to the new system of WTO.⁸⁰ Finally, the Appellate Body disagreed with the Panel's understanding indicated above.⁸¹

The effect of panel/AB reports of the WTO in Japan's domestic law remains ambiguous. Although Article 98(2) of the Constitution provides for the supremacy of treaties in Japan, Japanese courts so far denied the direct applicability of GATT.⁸²

as a "concordant, common and consistent" sequence of acts or pronouncements which is sufficient to establish a discernible pattern implying the agreement of the parties regarding interpretation.

⁷⁶Panel Report of Japan's Taxes on Alcoholic Beverages, WT/DS8/R, WT/DS10/R, WT/DS11/R (11 July 1996), para. 6.10.

⁷⁷*Ibid.*, *supra* note 75.

⁷⁸*Ibid.*

⁷⁹Article IX:2 of the WTO Agreement; this article also provides that such decisions shall be taken by a three-fourths majority of Members.

⁸⁰Article XVI:1 of the WTO Agreement; para.1(b)(iv) of the language of Annex 1A incorporating the GATT 1994.

⁸¹Panel reports adopted by the GATT CONTRACTING PARTIES and the DSB of the WTO constitute subsequent practice in a specific case as that phrase used in Article 31 of the Vienna Convention, and adopted panel reports in themselves constitute other decisions of the CONTRACTING PARTIES to GATT 1947 (for the purpose of para. 1(b)(iv) of the Annex 1A incorporating the GATT 1994 into the WTO Agreement), see *supra* note 75.

⁸²See *supra* note 52 (the *Kobe Jewellery* case) and also *supra* note 54, 55 and 56 (the *Kyoto Necktie* case).

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If, however, the GATT/WTO Agreement is held to be directly applicable, Japanese courts are more likely to rely on the panel/AB reports as authoritative aid of interpretation. Whether this is going to be the case remains to be seen.

Chapter 7. CASE STUDIES: JAPANESE TRADE DISPUTES UNDER GATT - A TRANSFORMATION IN JAPAN'S POLICY ON DISPUTE SETTLEMENTS

Introduction

The aim of this and the next chapter is to examine key cases in which Japan has been involved under the GATT/WTO system.¹ This examination attempt to demonstrate a significant transformation in Japan's policy on trade dispute settlement. To begin with, this chapter will analyse the GATT panel reports, while the next chapter will examine those of WTO. The main conclusion is to be drawn from this case study is that there is a marked degree of change in Japan's attitude towards dispute settlement under those systems.

An attempt has been made to find out whether any change can be discerned in Japan's attitude towards trade dispute settlement, for example, a preference for a particular means of settlement (e.g. bilateral or multilateral; political/pragmatic or legalistic) under the GATT/WTO system. Another no less important concern of this analysis is to examine how GATT/WTO panels and appellate bodies handled those cases under the respective dispute settlement mechanism, i.e. the "old" GATT and the "new" WTO (under which "judicialisation" had emerged both constitutionally and institutionally as discussed in Part I of the thesis).

If one looks at those cases in which Japan was involved, one may notice a number of interesting indication reflecting a transformation of Japanese policy regarding trade disputes. For example, one may recall two disputes which were originally initiated by the U.S. Section 301 investigation (or its "threat"): the dispute over semiconductors ('85) whose bilateral settlement propelled another dispute brought by the EC on the same products, and the "Japan Auto" dispute ('95). In the former, Japan did not take the U.S. claim, which was under the investigation of Section 301, to the GATT panel where a multilateral solution was available. In other words,

¹For the purpose of this study, only those cases which, I believe, are important in Japanese GATT/WTO dispute settlement history have been selected for examination. Nonetheless, other Japanese disputes under GATT/WTO, are exhibited in Appendix IV at the end of the thesis, and will be referred to whenever necessary.

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Japan yielded to U.S. unilateral measures under Section 301. Like other disputes with the U.S. which were initiated with Section 301 investigation, Japan eventually signed to a bilateral arrangement concerning the trade at issue. Japanese behaviour in this case could be regarded as "conventional". Whereas, in the latter case, Japan did take action against the U.S. demand under the "threat" of Section 301. In other words, without yielding in obedience, Japan brought the U.S. claim to the multilateral table, i.e. the WTO dispute settlement system. Japan, therefore, marked a new approach to dispute settlements under the WTO. What were the reasons or factors behind this new progressive attitude taken by Japan? To answer this question, in this and the next chapters, the key cases and disputes selected will be scrutinised for the purpose of demonstrating how Japanese policy on dispute settlement evolved. To make the case studies more comprehensible, it is essential for us to widen our focus not only on those key disputes which produced a legal ruling but also on those disputes which were settled bilaterally or conceded as well as complaints withdrawn or abandoned. By touching upon those secondary or peripheral disputes, which will help to fill in the gaps between the key cases, we shall be able to see more clearly the transformation in Japan's policy on dispute settlement.

7. 1. Japan's Experience of GATT Disputes²

7. 1. 1. Japan as a "Respondent"

This type of cases/disputes in which Japan has been involved as a "respondent" indicated that Japan preferred to reach a bilateral settlement especially during the GATT period.³ This has been the typical pattern in Japan's attitude towards international trade disputes. Nevertheless, this Japanese stance towards resolving trade disputes often turned out to produce a negative result. One could look at this in two different respects, political and economic. Japan has never attained the status of a leading political power internationally, whereas it has obtained international economic status during the 80's. Japan, however, was not even in the upper league in the world economic scene before then. That being the case, one could imagine that Japan might have had little negotiating power, either economically or politically (when the dispute settlement rule was more "power-oriented"), to settle trade disputes with other contracting parties until the establishment of its global economic status in the 80's (when that system had been progressing towards a "rule-oriented" nature, i.e.

²For instance, GATT, Analytical Index, 5th ed., Geneva, 1989 (prepared by E.- U. Petersmann); GATT, Analytical Index : Guide to GATT Law and Practice, 6th ed., Geneva, 1994 (prepared by Amelia Porges) at pp. 719-34; Hudec, Robert E, Enforcing International Law - The Evolution of Modern GATT Legal System [hereinafter, the "Enforcing"], Butterworths Legal Publishers, Salem, New Hampshire, 1993 at 367; R.E. Hudec, The GATT Legal System and World Trade Diplomacy, 2nd ed., Salem, New Hampshire, Butterworth, 1990 (1st ed., New York, Praeger, 1975), at pp. 301-21; Hudec, "GATT Dispute Settlement after Tokyo Round: A Unfinished Business", 13 *Cornell Int'l L. J.* (1980) at 145; R.E. Hudec, "Legal Issues in US-EC Trade Policy: GATT Litigation 1960-1985", in *Issues in R. E. Baldwin et al. eds, US-EC Trade Relations*, 1988 at 17; J.H. Jackson, The World Trading System - Law and Policy of International Economic Relations [hereinafter, the "Trading System"], at pp. 98-103; Pescatore, Pierre, "Legal and Procedural Analysis" in Pescatore, Pierre., Davey, William J., and Lowenfeld, Andreas F., Handbook of GATT Dispute Settlement [hereinafter, the "Handbook"], Transnational Juris publications, Inc., New York, 1991 (the latest release is Release 8 in June 1997, ; Petersmann, P., Annex : GATT Dispute Settlement Proceedings under Article XXIII 1948-1990, in Petersmann, P., and Dr. Günther Jaenicke, Adjudication of International Trade Disputes in International and National Economic Law, Univ. Press Fribourg, Switzerland, 1992 at 407; U. S. I. T. C., I, 5-28.

³According to the WTO Secretariat statistics, there were 21 cases in which Japan had been involved as a "Respondent" during the GATT period [cf. the Uruguayan recourse to Article XXIII case is excluded in Japanese cases here] (The total number of disputes under GATT 1947 including Tokyo Round Code disputes: 312. This number excluded three cases which were initiated in 1995 when the co-existing arrangement regarding the Anti-dumping Code and the Subsidies Code). Among those 21 cases, Japan settled or conceded in 14 cases (67%) which is slightly higher rate than the rate appeared in Professor Hudec's statistics (65%). His statistics covered until the end of 1989, and total cases were 207, in *ibid.*, The Enforcing, at 301. Whereas, the WTO Secretariat statistics recorded 234 during that period.

depoliticised). This would be one of the factors which could explain why Japan did not achieve good result in settling trade disputes particularly during the GATT period. Bearing such background in mind, we shall set out case studies.

7.1.1.1. The Leather Case - Japanese Measures on Imports of Leather (United States v. Japan)⁴

Summary of Facts and Procedure:

In 1952, Japan imposed a system of quantitative restrictions on the importation of leather items. Until 1963, these restrictions had been justified and maintained as a balance-of-payments measure stipulated in GATT Article XII. Although Japan had acquired Article VIII status in the International Monetary Fund (IMF) in April 1984,⁵ and liberalised many leather items since that time, Japan continued to maintain restrictions on the import of certain semi-processed and finished leather items due to the small size and backward character of its enterprises (i.e. an economic reason) and, above all, due to the "Dowa" issue⁶ (i.e. a socio-political reason). Before the date of 31 March 1983, the expiration of the three-year settlement agreement reached on 23 February 1979 in the 1978 U. S. complaint,⁷ Japan and the U. S. had been negotiating

⁴Panel on Japanese Measures on Imports of Leather, BISD 31S/94 (1985) L/5623; for the summary of this case can be found in, R.E. Hudec, *The Enforcing*, *supra* note 2, pp. 508-509; Pescatore, P., et al., *The Handbook*, pp. CS57/1-2.

⁵Article VIII of the IMF defines general obligations of members. After World War II, most of member countries have been granted the status of Article XIV of the IMF (Transitional Arrangements) due to the lack of economic stability. Once a member recovered its economic stability, the IMF General Council recommends the members to meet with the general obligation of member under VIII. (The IMF was set up by the Bretton Woods Agreement of 1944 and came into operation in March 1947. The main objectives of the IMF is to encourage international co-operation in the monetary field and the removal of foreign exchange restrictions, to stabilise exchange rates and to facilitate a multilateral payments system between members countries).

⁶The origin of the "Dowa" issue goes back to the Tokugawa period (1615-1867). "Dowa" is a euphemism used for "Buraku" ("Burakumin", literally "village people", are people who belong to this group). The "Burakumin" are the descendants of people outside of the four classes (i.e. warriors, farmers, artisans and merchants) of the Tokugawa society. They were called "hinin" (no-mem) or "eta" (outcast, pariah) and engaged in certain occupations such as flayers, tanners and curriers. Despite the abolishment of those two discriminatory terms (*hinin* and *eta*) in August 1871 through a decree ("*mibun kaihourei*"- social position emancipation order), the social discrimination remained; see further Herzog, Peter J., *Japan's Pseudo-Democracy*, Japan Library, Kent, 1993, pp. 72-76; see also for Japan's explanation on "Dowa Problem", BISD 31S/94, *supra* note 4, para. 21.

⁷The 1978 GATT complaint was made by the U.S. on 20 July 1978 (L/4691). This

the issue but the negotiations ended unsuccessfully. On 25 February 1983, the U. S. requested the establishment of a panel on "Japanese Measures on Imports of Leather".⁸ Other countries such as Australia, the EC, India, New Zealand and Pakistan were also involved.

The U. S. legal claim was based on the following grounds: the quantitative restrictions on leather imports were in violation of GATT Article XI:1 (para. 15); the failure to publish quantitative restriction amounts and license holders, violated the "notice" requirements pursuant to GATT Article X:1 and XIII:3 (para. 16); the awarding of quantitative restrictions licenses through associations of domestic producers was in violation of the "reasonableness" requirement under GATT Article X:3 (para. 30). Those measures caused nullification and impairments of tariff concessions on leather.⁹

The U. S. further argued that, not only did Japanese import restrictions on leather constitute a *prima facie* case of nullification and impairment, they also represented actual nullification and impairment of the tariff bindings on leather which were stipulated in GATT Article II (para. 30). In addition, with respect to trade in leather, the U.S. pointed out that the substantial growth of its leather exports to the Far East market except Japan stood in contrast to the negligible rate in the growth of U. S. leather exports to Japan (para. 32).

Japan's arguments:

-A number of developed countries including Japan also maintained residual import restrictions, and thus it did not seem appropriate to seek a judgement on these issues simply from a legalistic point of view; In spite of the extremely difficult conditions of the Japanese leather industry due to complex domestic social problems and its low-level of competitiveness, Japan had made its maximum efforts to liberalise the import restrictions. (para. 17)

complaint was triggered by the U.S. Section 301 which was filed by the Tanners Council of America (TCA) in August 1977.

⁸Complaint was brought on 5 January 1983 (L/5440).

⁹This claim was contested by Japan separately.

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-No benefits accruing to the U. S. under the GATT has been nullified or impaired by Japan; In fact, Japan had opened a large quota for the U. S. and other countries, and furthermore it benefited them, which resulted in the steady increase in U. S. leather exports to Japan. (para. 18)

-The aim of the GATT was to expand trade and therefore the panel should have taken more substantive matters into account in its findings. (para. 19)

Japan claimed that the present case was deeply rooted in its history and thus the Hong Kong/European Community case¹⁰ cited by the U. S. was irrelevant to the present case. (para. 20)

-Except for the size of import quotas, the entire process of import quota allocation was published in the MITI Gazette as required in Article X:1; According to Article XIII:3(a), it did not require the name of import licence holders to be published and therefore, there was no obligation for Japan to publish the quantity of their import licences nor the size of unfilled import quota balances. (para. 27)

-The present system of import quota allocation has not violated Article X:3; Japan explained that " *...the fact that each tanner's demand was taken into account, the Tanners' Council of Japan was in no way controlled by the Government. Also tanners that were not members of the Council had actually been allocated quotas through the Council*"¹¹; Japan added that " *Importers wanted trade expansion and, once they had been allocated quotas, the Government had no intention of interfering with their transactions, nor did have any administrative means to do so*"¹²; Thus, Japan emphasised the rationality of its system of the import quota allocation. (para. 29)

¹⁰Quantitative Restrictions against Imports of Certain Products from Hong Kong, Report L/5511, adopted by the Council on 12 July 1983 (C/M/170) in BISD 30S/129 (1984).

¹¹BISD 31S/94 (1985), *supra* note 4, para. 29.

¹²*Ibid.*

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-The restriction on certain types of sheep, lamb, goat and kid leather had already been liberalised; the import quotas on sheep, lamb, goat and kid leather, the tariff on which were not bound. In other words, these items in the present case were not the object of tariff concessions; Japan, therefore, neither nullified nor impaired the benefits of the U.S. under Article II in connection with these items. (para. 31)

-Regardless of the different needs of the Japanese market, the concept of regarding the Far East as one market was impractical, and which was one of the reasons why U.S. leather was not imported in large quantities to Japan, in comparison with the quantity imported to other countries such as the Republic of China, the Republic of Korea, Taiwan and Hong Kong. (para. 35) Furthermore, Japan considered that the Japanese market was sufficiently open to the U.S. For instance, Japan showed an increase of leather imports, i.e. from US\$2 million in 1978 to US\$9 million in 1982 which means an increase of 4.5-fold (*c.f.* U.S. leather during the same period: a 1.9-fold increase world-wide; 3-fold increase to Italy; 3.5-fold increase to the Federal Republic of Germany); In fact, U.S. leather exports to France and the United Kingdom has decreased during the same period. Moreover, a considerable portion of the quotas available to the U.S. was unused; The problem can be found in the U.S. suppliers who did not make efforts to meet the demands of Japanese market, i.e. "*they had not carried out appropriate research and development and quality improvement efforts and had not, unlike European suppliers, met detailed requirements concerning trading lot, delivery time, etc.*" (para. 36)

Summary of Findings and Conclusions:

A panel made the following decisions:

-Japanese quantitative restrictions violated GATT Article XI:1.

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-Japan did not invoke any justification recognised by the GATT rules so as to maintain its quantitative restrictions, thereby the panel could not consider a possible justification under GATT Article XIX. Furthermore, the special historical, cultural, and socio-economic circumstances mentioned by Japan were deemed to be insufficient justification for its measures in dispute.¹³

-According to the established GATT practice,¹⁴ Japanese restrictions were found to be illegal and therefore constituted a *prima facie* case of "nullification and impairment" of the U. S. benefits under the GATT.¹⁵

-The quantitative restrictions which caused a preventive effect as indicated by market data analysis, made the U. S. unable to fill the quota allocated by Japan. Japan, therefore, did not disapprove "nullification and impairment".¹⁶

-Even though there is no substantial evidence to prove the existence of an actual trade restraint, the quantitative restrictions should be presumed to cause "nullification and impairment" not only because of mandatory quantitative restriction, affecting the volume of trade, but also for other reasons such as increased transaction costs and growing uncertainties affecting investment.¹⁷

-It became unnecessary to rule on claims with respect to the administration of quantitative restrictions, or on claims with regard to "nullification and

¹³*Ibid.*, para. 44.

¹⁴Annex to Understanding Regarding Notification, Consultation, Dispute Settlement and Surveillance (BISD 26S/215) [hereinafter, the "Annex to 1979 Understanding"], para. 5, which stated as follows:

"A *prima facie* case of nullification or impairment would *ipso facto* require consideration of whether the circumstances are serious enough to justify the authorisation of suspension of concessions or obligations, if the contracting party bringing the complaint so requests. This means that there is normally a presumption that a breach of the rules has an adverse impact on other contracting parties, and in such cases, it is up to the contracting parties against whom the complaint has been brought to rebut the charge"; cf. DSU 3.8.

¹⁵*Ibid.*, *supra* note 8, para. 46.

¹⁶"..., it was up to Japan to rebut the presumption that nullification or impairment had actually occurred." in *ibid.*, para. 47.

¹⁷*Ibid.*, para. 55.

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impairment" of tariff concessions because the panel had ruled that quantitative restriction violated GATT Article XI:1.

-The panel suggested that Japan should eliminate its quantitative import restrictions and conform with the GATT provisions.¹⁸

-The panel recognised that Japan faced difficulties in eliminating its quantitative restrictions on leather immediately, but noted that "*the first objective ... is to secure the withdrawal of the measures concerned if these are found to be inconsistent with the General Agreement*".¹⁹ The panel left the final decision to the Council whether or not Japan should be provided a certain amount of time progressively to eliminate the restrictions in question.²⁰ The panel suggested that the GATT Council should consider giving Japan extra time to comply with the panel decision because of a particular social problems.²¹ Subsequently, the GATT Council made a ruling in May 1984.²² A Substantial number of delegations pronounced reservations regarding granting extra time for compliance in favour of Japan.²³

¹⁸*Ibid.*, para. 59.

¹⁹*Ibid.* para. 60 (this citation is originally from the Annex to 1979 Understanding, *supra* note 13, at para. 4.)

²⁰*Ibid.*, para. 60.

²¹L/5623 (2 March 1984) in BISD 31S/94, *supra* note 4.

²²Report was adopted on 15-16 May 1984 (C/M/178).

²³Cf. For example, the WTO provided a strict time constraint for the implementation of DSB's recommendations and rulings (WT/DSB/M/26). In Japan - Taxes on Alcoholic Beverages case, Japan indicated that it would be able to implement within a "reasonable period of time". Nonetheless, in the absence of an agreement under Article 21(3)(b) of the DSU, the U.S. requested that the "reasonable period of time" should be determined through binding arbitration as is provided by Article 21(3)(c). Finally, the Arbitrator (Julio Lacarte-Muró) concluded that a "reasonable period of time" within the meaning of Article 21(3)(c) of the DSU for Japan to implement the recommendations and rulings of the DSB (1 Nov. 1996) in the present case is 15 months. (In almost all cases in which an arbitrator has concluded the "reasonable period of time" to be "15 months". Those cases are, for instance, the Canadian Periodical case (WT/DS31); strictly speaking, "15 months and one week" was given in the EC Banana case (WT/DS27); India Patent case (WT/DS50); the EC Hormones case (WT/DS26 and WT/DS48) (as of June 1998). Exceptionally, the arbitrator concluded the "reasonable period of time" to be 12 months in the Indonesian National Car case, see WT/DS54/15; WT/DS55/14; WT/DS59/13; WT/DS64/12 (7 December 1998).

After the immediate removal of some quantitative restrictions, Japan proposed withdrawal of tariff bindings and replacing quantitative restrictions with GATT lawful tariff quotas. The parties agreed on a settlement: (instead of liberalising its leather market) new tariff concessions by Japan on some U.S. exports as partial compensations for withdrawal of tariff bindings, and other compensation in the form of a discriminatory increase in the U.S. tariff against \$24 million of Japanese exports. On 1 April 1986, quantitative restrictions on leather products were replaced by tariff quotas which were considered as GATT lawful.²⁴ Later, Japan enquired about the legality of an ongoing discriminatory tariff increase by the U. S. under the GATT, but Japan stopped pursuing the matter further.²⁵

Remarks on the case:

1. The Panel's stance - a more legalistic approach?:

The panel insisted on a strict legalistic approach throughout the proceedings to settle the present case. As mentioned, however, the Japanese justification for its import restriction was not based on a specific provision of the GATT but on a domestic social problem. Although the panel took the argument into account, the panel also noted a panel report which had been adopted by the CPs in 1983.²⁶ In this panel report, the panel had concluded "... *that such matters [the social and economic conditions] did not come within the purview of Article XI and XIII of the GATT, and in this instance concluded that they lay outside its consideration.*"²⁷ Accordingly, based on that practice, the panel found that the import restrictions imposed by Japan contravened Article XI:1. Thus, the panel avoided taking into consideration each contracting party's special circumstances. In the end, the panel followed its legalistic approach to make a decision in this case.

2. Presumption of a *Prima Facie* Case of "Nullification or Impairment" and Possibility of Rebuttal:

²⁴C/M/191 (17-19 July 1985).

²⁵L/5978 (11 April 1986).

²⁶Panel report on Quantitative Restrictions against Imports of Certain Products from Hong Kong in BISD 30S/129 (1985).

²⁷*Ibid.*, para. 27.

In the present case, the panel noted that, according to the established GATT practice,²⁸ it would be possible for Japan to rebut the presumption of a *prima facie* case of "nullification or impairment" if Japan could provide a detailed justification to prove the GATT legality of Japan's measures at issue. In this case, the panel stated, however, that the Japanese arguments provided were insufficient to rebut the presumption that the Japanese import restrictions on imports of leather had nullified and impaired the U. S. benefits anticipated under Article XI.²⁹ Therefore, it was understood that the panel had, at least, examined the justification made by Japan in the present case although, as transpired, the result was unfavourable to Japan.

Was the panel reasonable in its consideration of the GATT rule regarding the possibility of rebuttal concerning a *prima facie* case of "nullification or impairment"? Here, there are a few points to be noted concerning this question. First of all, the interpretation and application of *prima facie* nullification or impairment under Article XXIII should be examined. The panel report on Uruguayan Recourse to GATT Article XXIII³⁰ (the "Uruguayan case") noted that "...in a case where there is a clear infringement of the provision of the General Agreement, ..., the action would, *prima facie*, constitute a case of nullification or impairment ...".³¹ Furthermore, the Annex to Understanding Regarding Notification, Consultation, Dispute Settlement and Surveillance³² (the Annex to 1979 Understanding) had confirmed the interpretation made in the Uruguayan case. In fact, in the present case, the panel affirmed the possibility of rebuttal based on the Annex to 1979 Understanding. After the Superfund Taxes case,³³ however, the panel denied the interpretation that had been supported in both the Uruguayan case and the Annex to 1979 Understanding. In short, the main point made in the Superfund Taxes case was laid in provision 4 of the Annex to the 1979 Understanding which defined that "*the first objective of the*

²⁸*Ibid.*, *supra* note 19.

²⁹BISD 31S/94 (1985), *supra* note 4, para. 56.

³⁰"Uruguayan Recourse to Article XXIII" (L/1923) in BISD 11S/95 (1962).

³¹*Ibid.*, para. 15.

³²*Ibid.*, *supra* note 14.

³³"Mexico, Canada & European Community v. United States: Taxes on Petroleum and Certain Imported Substances Case [hereinafter, the "Superfund" Taxes] in BISD 34S/136 (1988).

*CONTRACTING PARTIES is usually to secure the withdrawal of the measures concerned if these are found to be inconsistent with the General Agreement".*³⁴

Thus, this statement meant that in case of a GATT illegal act, such an act should be amended without reference to any influence on trade. On the other hand, as explained earlier, provision 5 of the Annex to the 1979 Understanding only defined whether or not a party could claim compensational measures after finding "nullification or impairment". In other words, compensational measures would not be provided if a responding party could prove that a situation was not serious enough as to justify seeking for compensation. To sum up, one may note that there seemed to be an ambiguous terminology (i.e. "presumption of *prima facie*") which might have caused confusion in applying the GATT rules in the present case. According to the interpretation of the Annex to 1979 Understanding, the possibility of rebuttal for *prima facie* nullification or impairment under Article XXIII would not be allowed (i.e. the interpretation made in the Superfund Tax case) though there seemed to be room for rebutting. In practice, however, no rebuttal has ever been accepted.³⁵

3. A few points to be noted concerning the report:

First, in the panel findings, the panel noted that "*Japan had not invoked any provision of the General Agreement to justify the maintenance of the import restrictions on leather*".³⁶ On one hand, the panel noted that "*The Panel decided that in such circumstances it was not for it to establish whether the present measures would be justified under any GATT provision or provisions*".³⁷ The panel, however, made a decision on the present measures that " *... these provisions did not provide such a justification for import restrictions*".³⁸ Japan did not simply rebut the U.S. claim to justify its measures in dispute, which was perhaps because of domestic

³⁴*Ibid.*, *supra* note 14, para. 4.

³⁵According to Article 3.8 of the DSU, in the event that there is a presumption of nullification or impairment (a breach of the rules which has an adverse impact on other Member parties to a covered agreement), it shall be up to the respondent to rebut the charge.

³⁶*Ibid.*, *supra* note 14, para. 44.

³⁷*Ibid.*

³⁸*Ibid.*

issues, i.e. to avoid a difficult social domestic problem by protecting the leather industry (which led to losing this case) rather than economic losses.

Second, in spite of the fact that the panel acknowledged the growth of U. S. leather exports to Japan by presenting trade figures,³⁹ the panel came to a conclusion by noting that "*However, the Panel could not escape the conclusion that the import restrictions were maintained in order to restrict imports, including imports from the United States*".⁴⁰ The panel further explained why it arrived at such a conclusion by stating: "... , *while the Japanese market was not fully comparable to other markets in East Asia, the evidence relating to these markets still tended to support the view that the Japanese restrictions limited United States' exports of leather to its market*".⁴¹ What relation did the U. S. trade export figures to East Asia, excluding Japan, have to do with U. S. exports to Japan and the Japanese import restrictions? On this point, it might be reasonable to state that the trade figures were not an important criterion in explaining the impact of U. S. exports to Japan which had allegedly been caused by the Japanese import restrictions.

Third, the way in which the panel dealt with the Japanese arguments (i.e. that the Japanese quota did not limit U. S. exports to Japan). The arguments were based on the fact that the U. S. exporters had not fulfilled their large quota. Could Japan prove that the Japanese import restriction did not affect U. S. exports? In the present case, although the panel said that "*these consisted of contradictory assertions by the two parties that, by their nature, were difficult to evaluate*",⁴² the panel however made a judgement that the existence of the Japanese import restrictions had adversely affected the exports of the U. S. based on two main facts: "(i) *the U. S. was able to export large quantities of leather to other markets; (ii) other supplying countries had supported the arguments of the United States*".⁴³ Nonetheless, one might query whether or not those reasons were truly persuasive. An answer would possibly be

³⁹*Ibid.*, para. 49.

⁴⁰*Ibid.*, para. 53.

⁴¹*Ibid.*, para. 54.

⁴²*Ibid.*

⁴³*Ibid.*

'no'. With regard to fact (i), it is unfair to take a view which considered the Far East to be one market. Each country has different preferences and demands regarding leather products. In addition, some countries have a favourable trade relationship with the U. S.⁴⁴ While, concerning fact (ii), this fact should not be taken into consideration as an important factor because, as noted in the panel report of the present case (i.e. " *...since its terms of reference were to examine the matter 'in the light of the relevant GATT provisions'* "⁴⁵), the Panel was essentially supposed to make a decision based on the consideration of the GATT provisions at issue. Nonetheless, as for the present case, the Panel made a decision based on the fact that one of the countries at issue shared assertions with other supplying countries. It seemed that the use of criterion (ii) in the present case was unreasonable in ruling on a case as stipulated in the GATT.

To conclude, the Japanese defence at the panel proceedings was unconvincing, because it based its arguments on domestic problems which needed to be tackled, whilst the Panel, for its part, manifested inconsistencies in its approach to arriving at its ruling. In short, this panel exhibited, to some extent, certain characteristics of the GATT cases, to some extent, such as the nature of old GATT dispute settlement mechanism coupled with Japan's characteristic stance towards the dispute settlement. The present issue was triggered by the threat of U.S. Section 301, and it proceeded to the GATT case. Unlike the first GATT claim by the U.S. on Japanese measures on imports of leather,⁴⁶ Japan did not accept the U.S. demand under the "threats" of Section 301 in the present case. In fact, this was because Japan's strong desire was to avoid a difficult social problem ("*Dowa*" issue) rather than economic losses, Japan was, as a consequence, defeated at the present panel. Lastly, with respect to the domestic situation, one might have imagined that the Japanese government intended to take advantage of foreign or international pressure, i.e. the GATT panel decision,

⁴⁴*Ibid.*, para. 35.

⁴⁵*Ibid.*, para. 44.

⁴⁶On 26 February 1979, the disputing parties notified the panel that a settlement had been reached, which was adopted on 6 November 1979 (C/M/135). The settlement included a three-year agreement granting larger quotas in some products and a commitment of progress in others.

in order to improve the problem both politically and socially at home (i.e. protectionist movements) avoiding facing much domestic tension in the process, as international pressures rather than the Japanese government could be blamed.

7.1.1.2. : The Alcoholic Beverage Case - Restrictions on Alcoholic Beverages (European Community v. Japan)⁴⁷

Summary of Facts and Procedure:

In July 1986, the EC filed a claim against the Japanese government regarding its practice of classifying alcoholic beverages into a number of categories and setting substantially different tax rates according to each category.⁴⁸ The EC argued that the practice was discriminatory against foreign products, which contravened Article III:1 and 2 of GATT. The parties to the dispute could not reach a settlement bilaterally, thus on 4 February 1987, a panel was established.⁴⁹

The present case dealt with the consistency of the Japanese liquor tax system⁵⁰ with the relevant GATT provisions. First of all, in this case, the panel clarified that the

⁴⁷Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages, BISD 34S/83-135 (1988) L/6216 (13 October 1987); for the summary of this case can be found in, R. E. Hudec, *The Enforcing*, *supra* note 1 at 538; P. Pescatore, et al., *The Handbook*, *supra* note 2, pp. CS63/1-/6.

⁴⁸Complaint was made on 5 November 1986 (L/6078).

⁴⁹C/M/206, item 7.

⁵⁰Japanese Liquor Tax Law (hereinafter, the "Liquor Tax Law") or "*Shuzeihou*" in Japanese classified liquors into 10 categories of which 6 categories were further classified into 13 sub-categories, and in the case of *sake* and whisky/brandy, into three extra grades (see, for the classification of liquors in Japan, C/M/206, Annex I at 128). Furthermore, each category was allocated a different tax rate subject to the Liquor Tax Law. In addition, the Liquor Tax Law was an excise tax, whose imposition was mainly based on quantity (but partially based on *ad valorem* tax).

According to the Liquor Tax Law, whiskies and brandies were *automatically* categorised into three different grades: special, first and second grades, based on certain standards such as the mixture ratio of ingredients (i.e. malt whisky, grain whisky, pure brandy, and alcohol content of whisky and brandy). Whereas, with respect to the grading of *sake*, producers could *voluntarily* selected its grading. In addition, the higher rates of specific tax were applied to higher grades subject to the Liquor Tax Law. With respect to wines, spirits (such as vodka, gin and rum) and liqueurs, according to the Liquor Tax Law, *ad valorem* taxes were applied instead of specific tax where the prices exceeded a certain threshold set for each category of alcoholic beverage (See, *ibid.*, Annex IV at 134). In this case, the tax rates were set higher under *ad valorem* taxes than specific taxes. Moreover, in case of the domestic products, the domestic producers could choose one of two methods in computing the price of taxation.

first and second sentences of GATT Article III:2 were applicable to the differentiation in internal tax among "like products" and also among "directly competitive or substitutable products". Second, this case clarified in what circumstances the differential taxation contravened the first and second sentences of GATT Article III:2.

The EC claimed that Japanese liquor tax system was inconsistent with GATT Article III based on six violations:

- "Almost all whiskies and brandies imported from the EC were classified as a special grade *automatically* and higher tax rates were applied, because these imported alcoholic beverages were made of pure ingredients like pure malt whiskies, pure grain whiskies and pure brandies. On the other hand, more than half of domestic whiskies and brandies (in fact, most of them are blended products) were classified as first or second grade and thus had applied lower tax rates. Accordingly, such a grading system contravened the first sentence of Article III:2;

- In general, wines, spirits and liqueurs imported from the EC were subjected to relatively higher *ad valorem* taxes in Japan than domestic like products, because the prices of those imported alcoholic beverages included import duties for the tax purpose. Therefore, such system in applying *ad valorem* taxes was in violation of the first sentence of Article III:2;

- There were different methods of calculating *ad valorem* tax for imported and domestic products. With respect to the calculation of taxable value for *ad valorem* tax, there was just one method of calculation available to imported products, whereas there were two methods of calculation available to

On the other hand, in the case of imported products, that price consisted of the CIF (i.e. an acronym of a trade term for Cost, Insurance, and Freight, or Charged in full) cost plus import duty. Furthermore, with respect to liqueurs and sparkling wines, higher tax rates were applied to these products in cases where they contained more than a certain ration of extract or non-volatile ingredient content. Nonetheless, specific tax rates were applied to *shochu*, of which rates were considerably low in comparison with the other liquors such as whiskies/brandies.

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domestic products. For this reason, in selecting the method, it could be reasonably said that domestic producers could choose whichever was the more favourable to them. Therefore, this discriminatory method of calculation was in violation of Article III:2 and the first sentence of Article III:4;

- In most of cases, liqueurs and sparkling wines imported from the EC were subject to higher specific tax, because these alcoholic beverages contained higher extract or non-volatile ingredient content, while some of the domestic products were subject to lower specific tax rates due to lower extract content. Therefore, such system of taxation based on extract content constituted a violation of Article III:2;

- *Shochu*, whisky/brandy and spirits (such as vodka, gin and rum) belonged to distilled liquors and, according to interpretative note to paragraph 2, second sentence of Article III:2, these alcoholic beverages were considered to be "directly competitive or substitutable products". Accordingly, the imposition of favourable specific tax rates to *shochu* was intended to provide protection to the domestic production of *shochu*. For this reason, such system was in violation of the second sentence of Article III:2; and,

- *Sake* and *shochu* (generalised as "Japanese traditional liquors") were not subject to *ad valorem* taxes although there were few exceptions. Whilst, wines and whiskies (i.e. "Western-style liquors"), which were above the non-taxable threshold in value, bore heavy *ad valorem* taxes. As a result, such a system constituted a violation of the second sentence of Article III:2.⁵¹

In addition to the above six complaints, the EC also claimed against Japanese labelling practices.⁵² According to the claim made by the EC, Japanese labelling

⁵¹BISD 34S/83, *supra* note 47, paras. 3.2 - 3.5.

⁵²*Ibid.*, para. 3.8.

practices on domestic wines and alcoholic beverages using English or French names contravened Article IX:6 which stipulated an obligation to co-operate in order to prevent the use of trade names in such manner as to misrepresent the true origin of a product.

Summary of Findings and Conclusions:

The panel concluded as follows:⁵³

- Violation of the first sentence of GATT Article III:2: the grading system; the application of *ad valorem* tax above the non-taxable threshold; and the taxation system according to extract content;

- Violation of the second sentence of GATT Article III:2: the application of extremely low rate of specific tax to *shochu* compared with other distilled liquors;

- Dismissal (non-violation claim): the method of calculation for *ad valorem* tax and the Japanese labelling practices; and

- The other issues claimed by the EC did not contravene the GATT.

The details of the decisions of Panel:

- The following group of products indicated were considered to be "like products": all of gins, vodka (including Japanese "*shochu*"), whisky and spirits similar to it, grape brandy, fruit brandy, classic liqueurs, unsweetened still wine, and sparkling wine;

- The first sentence of Article III:2, providing equal tax treatment of "like products," did not exempt different tax treatment within the classification of "like products" as regards the imposition of higher tax;

⁵³L/6216 in BISD 34S/83, *supra* note 47 at 151.

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-Several imports were taxed heavier than "like" domestic products which violated the first sentence of Article III:2;

-According to the first sentence of Article III:2, a different tax rate on "like products" was not permitted if such taxes were based on an objective characteristic of the product, such as its alcohol content. Furthermore, such rule could not justify differences of tax rate caused by a tax scale based on "extract content" where the tax was clearly not a tax on "extract" and where imports were disadvantaged by the non-uniformed tax scale;

-Various methods to calculate value for *ad valorem* tax did not violate Article III:2 of the GATT with no evidence that differences created lower values for domestic products;

-According to the second sentence of GATT Article III:2, the following product groups were "directly competitive" as defined in the Article: all distilled spirits, all liqueurs, and all still wines;

-Certain variations in the taxation on products within the larger groups produced a competitive disadvantage for imported products against "directly competitive" domestic products, and as a result, domestic products were protected, which violated the second sentence of GATT Article III:2;

-It is not required, under the second sentence of GATT Article III:2, to establish protective effect in order to prove influence on actual trade;

-Taxes inconsistent with criteria provided for in GATT Article III:2 for the purpose of adjusting tax according to criteria of ability-to-pay are not justified;

-Laws giving permission to apply Western words and images on labels were not proved to constitute a violation of GATT Article IX:6, in the absence of showing either harmful influence or non-co-operation by the government.

As a result, although Japan disagreed with the rulings concerning Article III:2, it did not block adoption.⁵⁴ Japan amended its liquor tax so as to fulfil the recommendations of the GATT Panel. For instance, by a law effective as at 1 April 1989, Japan abolished its *ad valorem* tax on the beverages affected by this recommendation, its tax based on extract content, and its "grading system" used in classification. Japan also reduced the tax differential, i.e. lowered the tax on whiskies/brandies, while raising the tax on shochu.⁵⁵ Nevertheless, in spite of the Japanese acceptance of the GATT rulings,⁵⁶ the EC was dissatisfied with the situation because Japan's implementation of the panel's decision did not remedy all material violations. In the meantime, Japan stated that the remaining issues were *de minimis*.⁵⁷

Remarks on the case:

i) The present and previous cases:

The main issue of the case under discussion was whether differential taxation among various liquors under the Liquor Tax Law constituted a violation of GATT Article III:2. In fact, there were other cases in which it was argued that differential tax or differential treatment by internal regulation among "like" or "directly competitive or substitutable" products were inconsistent with Article III:2, 4 or 5.⁵⁸ In those cases,

⁵⁴C/M/215 (10-11 November 1987).

⁵⁵L/6465 (2 February 1989).

⁵⁶Japan disagreed with the Panel's decision on Article III:2, nonetheless, did not block adoption of the report itself. In fact, Japan never blocked adoption of panels' report when it lost a panel (e.g., Leather case; Agriculture case; and Semiconductor case), which should be worth noted.

⁵⁷C/M/228, C/M/230 (Meetings of 8-9 February and 6 March 1989).

⁵⁸See, for example, the U.S. v. France (Auto Taxes), 12 September 1956 (L/520), for summary of this case see Hudec, *The Enforcing*, *supra* note 2, pp. 438-439; the U.S. v. the EC (Measures on Animal Feed Proteins), 27 April 1976 (C/M/113) BISD 25S/49 (1979), reported adopted on 14 March 1978 (C/M/124), also see *ibid.*, pp. 466-467; and the U.S. v. Spain (Measures concerning Domestic Sale of Soybean Oil), 1 November 1979 (L/4859), the ruling by Panel, L/5142 (17 June 1981) and L/5142/Corr.1 (22 June 1981) but not reproduced in BISD, namely, unadopted; also see *ibid.*, pp. 479-481.

however, the Panel did not make any significant statement regarding the issue of the applicability of Article III to differential treatment among products. The present case, however, was a case in which the Panel found violation of Article III:1 and 2, second sentence in respect of differential tax treatment among products. In addition, the approach taken by the Panel would also seem applicable to differential treatment by internal regulation among products under Article III:4. Hence, the Panel Report of the present case can be considered to be as a leading case on differential treatment among products by internal tax or internal regulation.

ii) Applicability of Article III:2 to differential taxation among products ("Origin Neutrality"):⁵⁹

Japan argued that "since there existed a substantial domestic production of products which were almost identical to the products of the EC, and both imported and domestic products were subject to the same taxation, there was accordingly, no discrimination in violation of GATT Article III:1 and 2."⁶⁰ With respect to this point, however, the Panel supported the EC's view.⁶¹ Namely, the Panel concluded that the conformity of internal taxes with Article III:2 required to be scrutinised closely determine the following: first, whether the imported and domestic products are "like" or "directly competitive or substitutable"; second, if the internal taxation was found discriminatory among "like" products, it would constitute a violation of Article III:2, first sentence, and if the internal taxation was found protective among "directly competitive or substitutable" products, it would constitute a violation of Article III:2, second sentence.

⁵⁹BISD 34S/83, *supra* note 47, para. 5.5; see the Japan Alcohol-II for the "origin-neutral" test, namely, all shochu is treated alike (domestically produced as well as imported, e.g. from Korea) and also all whiskey is treated alike. In other words, it is treated *on the basis of the product specification* not on the basis of origin; also see the Indonesian National Car case in Appendix III to the thesis [WT/DS54/R; WT/DS55/R; WT/DS59/R; WT/DS64/R (2 July 1998)], for the examination of the issue under two pillars, i.e. first the "origin-neutral" basis (focusing on whether cars "like") and second, the "origin-specific" basis (local content rules, etc.). Panel found a violation under both tests.

⁶⁰*Ibid.*, para 3.11.

⁶¹*Ibid.*, paras. 3.5-3.6.

The Panel, furthermore, stated four grounds on which the above interpretation of Article III:2 was based. Those were: 1) the context of Article III:2; 2) only literal interpretation of Article III:2 as prohibiting "internal tax specialisation" discriminating against "like" products could ensure that reasonable expectation of competitive benefits accruing under tariff concessions would not be nullified or impaired by internal tax discrimination against like products; 3) as drafting history confirmed, Article III:2 was designed with the intention that internal taxes on goods should not be used as a means of protection; and 4) GATT practice in the application of Article III further indicated and also supported the interpretation of the present case.⁶² The reasoning of the Panel would be convincing except for ground 1) above. It is because ground 1) dealt with only Article III:2, first sentence. Moreover, it was not appropriate for the Panel to refer to the GATT precedents, because those cases cited were only concerned with the examination of likeness, direct competitiveness or substitutability of the products in question, only as the question of the order for initiating an examination.⁶³ Nonetheless, by and large, the Panel's interpretation of Article III:2 seemed to be reasonable.

iii) Range of "Like Products":

With regard to the issue of "like products", Japan contended that two other points to be taken into consideration as criteria in determining "like product" were: i) minor differences in taste, colour and other properties; and ii) price differentials of products. With respect to point i), the Panel concluded that "minor differences in taste, colour and other properties did not prevent products qualifying as 'like products' ".⁶⁴ In this sense, the Panel agreed with the positions adopted in previous Panel reports.⁶⁵ Therefore, in the present case, the Panel did not take into account differences in quality of whisky and liqueurs, on which Japan had insisted. In addition, the Panel

⁶²*Ibid.*, para. 5.5. a), b), c) and d).

⁶³See **BISD 25S/49 (1979)**, Mexico, Canada and the EC v. the U. S. - Taxes On Petroleum And Certain Imported Substances ["Superfund" Taxes] in **BISD 34S/136 (1988)**, see also Hudec, *The Enforcing*, *supra* note 2, pp. 535-537.

⁶⁴**BISD 34S/83**, *supra* note 47, para. 5.6; see also the finding of previous panel report adopted in *Brazil v. Spain: Tariff Treatment of Unroasted Coffee* in **BISD 28S/102, 112, (1982)**.

⁶⁵*Ibid.*, **BISD 28S/102**.

noted that a certain panel report had been criticised by contracting parties in that the interpretation of "like products", defined as "more or less the same products" was too strict. Accordingly, bearing such criticisms in mind, the Panel clarified the term "like products" stipulated in Article III not only as "identical" or "equal" products, but also as products sharing "similar" qualities.⁶⁶

With regard to point ii), the Panel did not consider price differentials to be one factor in examining "like products". It was because that "... *such an interpretation would run counter to the objective of Article III:2 to avoid that discriminatory or protective internal taxation of imported products which would distort price competition with domestic like or directly competitive products, for instance by creating different price and consumer categories and hardening consumer preferences for traditional home products*".⁶⁷ Nonetheless, the Panel reasoning in the present case might be unacceptable in cases where price differentials of products already exist. Even in such cases, if a higher rate of internal tax applied to high-priced products, it is reasonable to say that the more expensive imported products would be at a disadvantage in comparison to the less expensive like domestic products. It, therefore, seemed fair that the Panel did not consider price differential of the products in question in determining "like products".

Nonetheless, it should be noted that the Panel referred to a "likeness" between Group A *shochu* and vodka.⁶⁸ The EC, however, asserted only that differential tax treatment between *shochu* and other distilled liquor violated Article III:2, second sentence. In this sense, the Panel went beyond the claim made by the EC. In fact, this part of the Panel report seems irrelevant to the Panel resolution of this dispute (i.e. beyond the scope of panel terms of reference). As a result, with respect to the EC's allegation, the Panel simply expressed its agreement with the argument made by the EC. One might assume that such behaviour on the Panel's part was taken in order to avoid an

⁶⁶*Ibid.*

⁶⁷BISD 34S/83, *supra* note 47, para. 5.9. b).

⁶⁸*Ibid.*, para. 5.7.

assertive conclusion of the case. Accordingly, the panel investigation of this dispute might have left uncertainty in this Panel report.

iv) Criteria for determining violation of GATT Article III:2, first sentence:

With respect to this point, the Panel insisted upon a literal interpretation of Article III:2, first sentence. Being based on this approach, the Panel concluded that the provision of Article III:2, first sentence prohibited even different tax treatment of like products through the classification of tax categories. Furthermore, the Panel also referred to the fact that imported wines and other liquors being subject to *ad valorem* tax, and liqueurs and sparkling wines bearing taxation according to extract content were subjected to internal taxes in excess of those applied to domestic "like products". The Panel thus concluded that this differential taxation between these "like products" was inconsistent with Article III:2, first sentence.

This differential taxation could not be justified under any of the exception clauses of the GATT. It may be noted that the position taken by the Panel in determining breach of Article III:2, first sentence was because of the following reasons: Judging from the Panel's conclusion of the present case, the Panel seemed to take the view that in cases where some imported products exist in categories subject to higher tax rates, while domestic "like products" exist in the lower taxed categories, such differential treatment of internal taxes among "like products", regardless of a *de facto* discriminatory effect, constitutes a breach of Article III:2, first sentence, in the absence of justification under any of the exception clauses under GATT; On the other hand, with respect to whiskies/brandies were subject to the grading system, the Panel referred to the fact that as a result of differential taxation, almost all whiskies/brandies subject to higher tax rates, whereas more than half of these items produced domestically enjoyed benefits through considerably lower tax rates. It seemed that the Panel, therefore, could be inconsistent in deciding a breach of Article III:2, first sentence.

Nevertheless, the Panel report discussed above could be interpreted as simply referring to an unreasonable discriminatory effect on the products of the EC as a

result of Japanese grading system. The Panel, therefore, did not state a necessary condition for finding a violation of the GATT Article III:2, first sentence. Furthermore, according to two previous cases,⁶⁹ it might be unnecessary to check the position of imported products and domestic products in a question relating to a finding of a contravention of Article III:2, first sentence. Perhaps, it can be assumed that the Panel has been aware of the precedents.

With respect to the general rule of different tax treatment of "like products", would there be any circumstances in which such treatment was compatible with the GATT? The Panel's reply to this question that there are such circumstances allowed under the GATT and the Panel indicated the following exceptional circumstances: i) Article II:2 permitted non-discriminatory taxation "of an article from which the imported product has been manufactured or produced in whole or in part";⁷⁰ ii) Article XX(b), defining "general exceptions", could permit discriminatory taxation in cases where it was "necessary to protect human, animal or plant life or health".⁷¹

With respect to these exceptions raised by the Panel, there would still be some doubt as to the Panel's interpretation of them. For example, Article II:2 indicates exceptions to Article II:1, but not to Article III. In addition, Article II:2(a) requires the compliance of the internal tax at issue with Article III:2. And thus in cases where any internal taxes were contrary to Article III:2 the requirements under Article II:2 would not be fulfilled. Whereas, with respect to the other exception under Article XX(b), one can note that the Panel has interpreted the requirements for application of this Article quite narrowly in some Panel reports, and therefore only a few exceptions have been permitted.⁷² As a result, judging from such a trend which strictly interprets

⁶⁹France v. Brazil - Internal Taxes in **BISD 2S/181 (1952)** at para. 16; the Superfund Taxes case, *supra* note 33.

⁷⁰**BISD 34S/83**, *supra* note 47, paras 5.9. and 5.13.

⁷¹*Ibid.*; cf. Note that, unlike the Japan Alcohol-I case, no attempt was made to justify the inconsistent measure under general exceptions of Article XX in the Alcohol-II case; see also, *infra* note 72.

⁷²For an example, see the U. S. - Section 337 of the Tariff Act of 1930 in **BISD 36S/345 (1989)** which denied applicability of Article XX:(d) of the GATT; Thailand - Restriction on Importation and Internal Taxes on Cigarettes in **BISD 37S/200 (1990)** which denied applicability of Article XX:(b) of the GATT; and for study of recent panel reports involved

Article XX, it is doubtful whether an exception under this Article is practical possibility.

The Panel found that alcoholic beverages, (i.e. vodka; whisky; grape brandy; fruit brandy; "classic" liqueurs; still wine; and sparkling wine), should be considered respectively as "like products" in terms of GATT Article III:2 in view of their similar properties, end-uses and usually uniform classification in tariff nomenclatures.⁷³ In addition, the Panel supported this finding by stating that such products were recognised by consumers as constituting "... a well defined and single product intended for drinking".⁷⁴ It is true that the precedents have defined the range of the "like products" on a case by case basis after examining a number of related factors. Furthermore, the criteria for scrutinising "like products" mentioned in the 1970 Working Party Report on Border Tax Adjustments⁷⁵ were as follows: "the product's end-uses in a given market, consumers' tastes and habits, and the product's properties, nature and quality".⁷⁶ In the present case, the Panel considered all these three criteria in defining "like products". In addition to them, the Panel also took tariff nomenclatures, as another criterion, which was based on the previous report.⁷⁷ To a certain extent, giving consideration to classifications of tariff nomenclatures would be effective in defining "like products" because such classifications in tariff nomenclatures represent recognition of the range of "like products" by a government.

Nonetheless, it would be understandable that the Panel's conclusion referred to the possibility of exceptional circumstances, i.e. different tax treatment of "like products" as being permissible. For example, there are cases in which different tax treatment of "like products" is necessary because of considerations of legitimate regulatory control (i.e. a sovereign issue). In this case, such treatment had nothing to do with

Article XX of the GATT, see Klabbbers, Jan., "Jurisprudence in International Law - Article XX of GATT - ", 26 J. W. T., No. 2 (1992) at 63.

⁷³BISD 34S/83, *supra* note 47, para. 5.6.

⁷⁴BISD 28S/102, 112, *supra* note 64, para. 4.7.

⁷⁵For "Working Party Report on Border Tax Adjustment" in BISD 18S/102 (1970).

⁷⁶*Ibid.*, para. 18.

⁷⁷See BISD 25S/49, *supra* note 63.

the aim of protection to domestic production. Thus, if such treatment (the different tax treatment among "like products") was found to constitute a violation of Article III:2, in spite of necessity based on legitimate reasons (i.e. a non-trade policy), it would amount to an undue interference with a domestic policy of each contract party. Accordingly, it would be a better alternative to seek an exception under Article III instead of referring to Article XX⁷⁸ in order to avoid a charge of violation in the case of different taxation among "like products" with no domestic protective effect and with GATT lawful reason.

(v) Range of "Directly Competitive or Substitutable Products":

According to the interpretative note to Article III:2, the expression "directly competitive or substitutable products" is considered to have a wider range than that of "like products". For instance, in a case in which direct competitiveness or substitutability is found even among different products, the requirement that it constitutes "directly competitive or substitutable products" is considered to be fulfilled.⁷⁹ As for the present case, the Panel concluded that alcoholic beverages, such as distilled liquors, liqueurs, wines, and sparkling wines, could be considered to be respectively "directly competitive or substitutable products" in terms of Article III:2, second sentence. With respect to such a conclusion by the Panel, the legal basis in which the Panel relied upon was implicit. Nonetheless, it could be assumed that the Panel was deemed to have considered various consumer habits vis-à-vis these products, apart from the competitive inter-relationship and substitutability respectively within these products.⁸⁰ In this respect, one could evaluate the fact that the Panel limited the range of these products by taking various consumers' habits into

⁷⁸For an example, see *Canada v. the U. S. - Measures Affecting Alcoholic And Malt Beverages* in **BISD 39S/206**, and also in *Pescatore, The Handbook, supra* note 2, pp. 217-223.

⁷⁹**BISD 25S/49**, *supra* note 63, para. 4.3.; for another example, see the *U. S. v. Spain: Measures Concerning Domestic Sale Of Soybean Oil* in **L/5142 (17 June 1981)** and **L/5142/Corr. (22 June 1981)**, which was not adopted, thus not printed in the **BISD**. In the latter case, for instance, skimmed milk and vegetable protein products were considered "directly competitive and substitutable products" because of substitutability from their end use viewpoint.

⁸⁰**BISD 34S/83**, *supra* note 47, para. 5.7.

consideration, was to prevent the possibility of the range of "directly competitive and substitutable products" growing infinitely.

(vi) Criteria for determining a violation of GATT Article III:2, second sentence:

The present case has clarified criteria for determining a violation of Article III:2, second sentence, since there had not been any previous cases where this Article applied. In the present case, the Panel emphasised that Article III:2, second sentence, prohibited the application of internal tax to imported or domestic products "so as to afford protection to domestic production", stipulated in the second sentence of Article III:2. Then, the Panel concluded that a violation of Article III:2, second sentence would be constituted only when the differential tax among "directly competitive or substitutable products" was established to cause the effect of affording protection to domestic production considering the particular circumstances of each respective case. Nonetheless, it is noteworthy that the Panel added "if there could be a *de minimis* level below which a tax difference ceased to have the protective effect prohibited by Article III:2, second sentence".⁸¹ In other words, if the level of the tax difference was merely a *de minimis*, this tax difference would not be deemed to constitute a violation of Article III:2, second sentence.

Furthermore, the criteria for determining inconsistency with Article III:2, first sentence could be more lenient than that for determining a violation of Article III:2, second sentence. This is simply because a violation of the first sentence of Article III:2 could be constituted by the mere existence of tax differentials among "like products" without a *de minimis* test. Whereas, the determination of a violation of the second sentence of Article III:2 would be more difficult because of, for instance, the following reasons. The wording used in the first and the second sentence in this Article is different. The concept of the phrase "directly competitive or substitutable products" tended to be interpreted wider in its scope and more extensively than that of "like products" in the first sentence of Article III:2. Therefore, for those reasons, the Panel may have narrowed and restricted cases in which different tax treatment

⁸¹*Ibid.*, para. 5.11. at 122.

among "directly competitive or substitutable products" constituted a violation of the second sentence of Article III:2, in comparison with cases where different treatment among "like products" breached the first sentence of Article III:2. Such interpretation of Article III:2, second sentence seems to be inconsistent.

The Panel, on the basis of the above interpretation of the second sentence of Article III:2, then turned to the application of considerable lower internal taxes imposed by Japan upon *shochu* than other "directly competitive and substitutable" distilled liquors, which had trade-distorting effects affording protection to domestic production of *shochu* contrary to Article III:2, second sentence. This conclusion was based on the following grounds⁸²: (i) the considerably lower specific tax rates on *shochu* than on imported distilled liquors and spirits⁸³; (ii) the imposition of high *ad valorem* taxes on imported distilled liquors and other spirits, as opposed to the non-existence of such taxes on *shochu*; (iii) the fact that *shochu* was almost exclusively produced in Japan. Furthermore, the (i) and (ii) grounds are factors which demonstrated a considerable difference in tax burden between *shochu* and other distilled liquors, and (iii) indicated almost all *shochu* were exclusively domestic products. Accordingly, it could be recognised that these factors afforded a protected effect prohibited to domestic products.

In the meantime, however, some points remain to be clarified. For example, are there any other factors to be considered apart from those two mentioned above, i.e. the proportion of imported products which bear heavy tax; the existence of a proper basis explaining differential tax treatment? Moreover, it should be noted that the Panel did not consider it necessary to examine the quantitative trade effects of the different taxation in order to answer the issue as to whether Japan afforded protection to domestic products contrary to Article III:2, second sentence.⁸⁴

⁸²*Ibid.*

⁸³See Annex III, BISD 34S/83, *supra* note 47.

⁸⁴*Ibid.*, *supra* note 82; the Panel, however, took an opposite position in the report of Spain - Measures Concerning Domestic Sale of Soybean Oil (the U.S. v. Spain - Measures Concerning Domestic Sale of Soybean Oil, *supra* note 79) in which the Panel concluded as follows: it is necessary to consider the adverse trade effect of the regulatory measure on

(vii) Justification - "Taxation according to tax-bearing ability": .

In the present case, with respect to different tax treatment under the grading system of whiskies and brandies, and the different tax burden between *shochu* and other distilled liquors, Japan argued that the existing tax rates were appropriate and consistent in terms of the fundamental taxation principle of Japan, that is, "taxation according to the tax bearing-ability" of the respective consumer.⁸⁵ The Panel examined whether these discriminatory or protective taxes were contrary to Article III:2 or could be justified by Japan's taxation principle, and came to a conclusion that the GATT did not provide for the possibility of justifying discriminatory or protective taxes inconsistent with Article III:2 on the grounds that they had been introduced for the purpose of "taxation according to the tax-bearing ability" of domestic consumers of imported and directly competitive domestic liquors.⁸⁶

This Panel's conclusion was based on the following grounds⁸⁷: (i) the GATT did not include a provision for such a far-reaching exception, i.e. "taxation according to tax-bearing ability", to Article III:2; (ii) the tax differentiation based on "taxation according to tax-bearing ability of respective consumers" with a view to maintaining or promoting certain production and consumption patterns could easily distort price-competition among "like" or "directly competitive" products by creating price differences and price-related consumer preferences; (iii) a national policy of "taxation according to tax-bearing ability" relied upon necessarily subjective assumptions about future competition and inevitably uncertain consumer responses, and did not necessitate discriminatory or protective taxation of imported products. Furthermore,

"directly competitive or substitutable products" in order to establish a violation of GATT Article III:1; and furthermore, if the trade volume of such products concerned were found to be increasing, in that case, no violation of GATT Article III would be established. In the end, the interpretation of Article III presented in the Panel report on the Spanish case was not adopted but was noted by the Council (L/5161, 26 June 1981). With regard to the Panel report of the present case, the Panel seemed to have rejected the interpretation of Article III made in the Spanish Soybean case. Instead, the Panel clarified that the protective effect of domestic production was presumed from the degree of tax difference and the proportion of imported directly competitive products without giving any consideration to an adverse trade effect in terms of trade volume.

⁸⁵BISD 34S/83, *supra* note 47, para. 3.10. (a), (b).

⁸⁶*Ibid.*, para. 5.13.

⁸⁷*Ibid.*

it could be pursued in many other ways in compliance with Article III:2. It should be noted that the Panel seems to have prohibited an internal tax policy ("taxation according to tax-bearing ability").⁸⁸ Nonetheless, it would not be appropriate for the Panel to make its own judgement on national tax policy or any kind of national policy as a general rule because of the sensitivity of sovereignty of the Contracting Parties. In this regards, it would have been reasonable enough for the Panel to have referred to the other grounds (i) and (iii) described above. Thus, the Panel could have avoided that criticism by simply giving those two reasonings.

In September 1995, once again, the EC accompanied by Canada and the U.S. requested panel investigation under the new WTO concerning Japan's Liquor Taxes Law ("*Shuzihou*").⁸⁹ According to the claimants, Japan's Liquor Tax discriminated against imports. This recent case will be analysed in the next chapter.

⁸⁸ This concept is common under Japanese tax laws and therefore Japan repeated the same argument (taxation according to tax bearing ability) even in the recent second panel on Japan Alcoholic Beverages case under WTO, see para. 4.152 in **WT/DS8/R; WT/DS10/R; WT/DS11/R (11 July 1996)**, *infra* note 89.

⁸⁹The EU lodged its first complaint with the WTO concerning the suspended case against Japanese Liquor taxes in the week 18th June 1995; further information can be found in, the Financial Times, "EU tackles Japan on liquor tax", 21 July 1995 at 4; "EU lodges Japanese liquor taxes complaint", 26 June 1995 at 3; more articles concerning this issue are, the Financial Times, "Tokyo under fire over tax rate on spirits", 1 February 1995 at 4; "Brittan to seek ruling on Japan's spirit taxes", 4 April 1995 at 3; "Scotch whiskey producers take on Tokyo", 18 May 1994 at 6, "WTO completes legal framework", 29 November 1995 at 5; for status of trade disputes brought to the WTO (as on 5 October 1995) see, the WTO, WTO Focus, No. 5, August-September 1995; a joint panel, as provided for in DSU 9.1, was established at the DSB meeting on 27 September 1995, for the Panel Report of the present case, **WT/DS8/R (Complaints by EC); WT/DS10/R (Complaints by Canada); WT/DS11/R (Complaints by the U.S.) (11 July 1996)**; Japan filed an appeal on 8 August 1996, for the report of Appellate Body, **WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R (4 October 1996)**.

7.1.1.3. The Agriculture Case - Restrictions on Certain Agricultural Products (United States v. Japan)⁹⁰

It is necessary to comprehend the nature of agricultural trade under the GATT before examining the case itself. The GATT provided an exceptional clause, Article XI:2(c), for granting an exception to general elimination of quantitative restrictions prescribed in Article XI:1. Nevertheless, in reality, contracting parties did not find any necessity to utilise this exceptional provision. Regulation of the GATT on agricultural trade, therefore, started losing not only its effectiveness but also its *raison d'être*.⁹¹ Bearing the circumstances in mind, this case will be analysed next.

⁹⁰Complaint was made on 15 July 1986 (C/M/201), however, under the auspices of GATT Article XXIII, the initial consultations were held in 1983, three years in advance of the complaint which was filed in 1986; Japan - Restrictions on Imports of Certain Agricultural Products, BISD 35S/163-245 (1988) L/6253 (22 March 1988); for the summary of this case can be found in, Hudec, *The Enforcing*, *supra* note 2, pp. 513-533, also in Pescatore, *The Handbook*, *supra* note 2, pp. CS67/1-1/6; for a commentary.

⁹¹To explain this situation, three points should be pointed out. First, with respect to most of the contracting parties except the U. S., they used to enforce import restrictions (i.e. import quota) for many agricultural products based on the reason of international payments under GATT Article XII. Nonetheless, this reason could justify the import restrictions only during a certain period (i.e., from just after the war until the beginning of the 1960's). With respect to the case of Japan, it had been permitted to invoke Article XII from 1955, which is the year when Japan became a contracting party to the GATT, up to 1963.* From the end of the 1950's, due to the sign of recovery of international payments of these contracting parties, they were unable to invoke Article XII and obliged to abolish import restrictions subject to Article XI:1. Nonetheless, in fact, even after their recovery of international payments, import restrictions remained on a number of agricultural products in those countries. Furthermore, those import restrictions were enforced without invoking the provision of exception for agricultural products defined in Article XI:2(c). As a result, these import restrictions remained in spite of their inconsistency with Article XI:1, and those restrictions are named "residual import restrictions".** Moreover, no exporting country brought a case involving these import restrictions to the GATT dispute settlement procedure despite a violation of the GATT rules. Why did not exporting countries bring a case to the GATT dispute settlement procedure for residual import restrictions?

One thing to be pointed out here is that it was unnecessary for the U. S. to invoke the provision of exemption under Article XI:2(c), because the U.S. had obtained a waiver, in 1955, under the Article XXV with respect to import restrictions of their agricultural products. Accordingly, the U.S. managed to acquire and protect its national interests. In the meantime, the influence from the acquirement of a waiver by the U.S. appeared to be losing the momentum for an elimination of the residual import restriction on agricultural products in other contracting parties. Furthermore, the other significant factor to be spelled out for the question was the introduction of a variable levy system by the EC. This system was recognised as a "grey-area measure" under the GATT and which was introduced in 1962 as part of Common Agricultural Policy (CAP) of the EC whose purpose was to administer import restrictions on agricultural products in a different arrangement from import quotas. Besides these import protections at the border ("Market Access" measures) on agricultural products, there was a contentious issue between the U. S. and the EC in "export subsidies"*** for agricultural products, which caused serious damage in the area of agricultural trade within the framework of the GATT rules initially planned. Bearing these

Summary of Facts and Procedure:

In 1986, the United States claimed that import restrictions put into practice by Japan on 12 agricultural products⁹² was in violation of GATT Article XI:1. The violation of Article XI:1 can be reasonably alleged because each one of import restrictions failed to observe, at least one or more of the seven criteria required for an exception to quantitative restriction to be accepted, as stipulated in Article XI:2(c)(i).⁹³ Eventually, on 27 October 1986, a panel was established at the U.S. request.⁹⁴ The main issues in the present case were:

- Whether import quotas on certain agricultural products maintained by Japan could be justified subject to Article XI:2(c)(i).
- Whether Article XI:1 could not be applied to the import monopolies provided for in Articles XVII and II:4.
- Whether import restrictions operated through import monopolies could be justified under the general exceptional provision in Article XX:(d).
- Whether import quotas administered by Japan were inconsistent with Articles X and XIII.

circumstances in mind, this case will be analysed.

*For interesting research on the issue of the membership of Japan to the GATT, Akaneya, Tatsuo., The Problem of Japanese Accession to the GATT - A Case Study in Regime Theory, University of Tokyo Press, Tokyo, 1992.

On 16 November 1960, the procedure was approved for dealing with "residual import restrictions" in **BISD 9S/18-20, and according to this procedure, any contracting parties maintaining "residual import restrictions" were required to notify lists of all items subject to those restrictions which were applying contrary to the provisions of the GATT to the Secretary-General of the GATT.

***Regarding the "Export Subsidies", especially two aspects should be considered, which were major issues of discussion with respect to agriculture at the Uruguay Round: (i) the amount of money a government spent on export subsidies; and, (ii) the volume of subsidised products (agricultural products in this particular case) that would be exported.

⁹²The Foodstuffs Control Law ("*Shokuryokanrihou*") made import quotas of 12 agricultural items effective in Japan. The twelve agricultural items are: (i) prepared and preserved milk and cream; (ii) processed cheese; (iii) lactose; (iv) dairy products preparations; (v) starch and inulin; (vi) glucose and other sugars, sugar products preparations; (vii) fruit purée and pastes, fruit pulp and certain fruit juices; (viii) prepared and preserved pineapple; (ix) tomato juice, tomato sauce and ketchup; (x) dried leguminous vegetable; (xi) groundnuts; and (xii) prepared and preserved bovine meat.

⁹³In advancing this case, there are four cases dealing with Article XI:2(c)(i) of the GATT, and those cases are as follows: Canadian Import Quotas on Eggs in **BISD 23S/91 (1977)**; EEC's Programme of Minimum Import Prices, Licences and Surety Deposits for Certain Processed Fruit and Vegetables in **BISD 25S/68 (1979)**; EEC's Restrictions on Imports of Apples from Chile in **BISD 27S/98 (1981)**; the United States' Prohibition of Imports of Tuna and Tuna Products from Canada in **BISD 29S/91 (1983)**.

⁹⁴C/M/202.

-What are "all relevant elements" in terms of reference to be considered by the Panel in this case?

Summary of Findings and Conclusions:

In 1988, Japan and the U.S. agreed on measures to implement the panel report. Japan, therefore, agreed to expand the quotas regarding two products whose restriction had been found unjustifiable for exemption under Article XI:2(c)(i). At first, Japan offered to adopt the panel decision concerning ten of the twelve products at issue excluding dairy products and starch, though, this offer was rejected.⁹⁵ Japan, furthermore, gaining support from several governments, disagreed with the decision by the panel with respect to state trading⁹⁶ and to perishability.⁹⁷ In addition, Japan also expressed the views that the compliance with the decisions on dairy products and starch would need more time to be implemented.⁹⁸ Concerning the two issues, Japan was reluctant to accept the panel's decisions. Japan, after all, had agreed to partly abolish quotas on dairy products. Nevertheless, in fact, Japan simply increased quotas on other dairy products. Japan took the same action as regards starch, that is, lowering the tariff quota for corn and other materials for producing starch.

To sum up, Japan merely reduced tariffs on agricultural products which were not in question in order to make up for the refusal to abolish the quotas on dairy products and starch.⁹⁹ In October 1992, Japan finally agreed with the US that it would increase the quotas of dairy products and starch for a period of three years. The reason behind the period of transition of three years proposed by Japan may be found in the fact that there was an ongoing UR negotiation at that time. A similar reaction can also be found in the implementation of the panel report on "Parts and

⁹⁵SR. 43/4 (Meeting of 2 Dec. 1987), SR. 43/6 (Meeting of 3 December 1987) respectively.

⁹⁶Restrictions on trade imposed through state trading operations are prohibited by Article XI:1 and also by the Ad Article of the General Agreement.

⁹⁷Exceptions of the Article XI:1 are provided in the second paragraph of the same article (Article XI:2); for this particular case, the criterion of the exception is dealt in Article XI:2.(c)(i) and the Ad Article on Paragraph 2(c).

⁹⁸GATT, GATT Activities 1991, Geneva, July 1992, at 67.

⁹⁹Japan stated that complete fulfilment in respect to dairy products and starch would have to suspend until the completion or result of the ongoing Uruguay Round. C/M/247 (Meeting of 6 February 1991).

Components" by the EC. In general, towards the end of the GATT system, a number of contracting parties maintained applications of their complaints awaiting the outcome of then ongoing UR negotiations.

Remarks on the case:

In this case, the GATT panel made an important contribution in its serious attempt to interpret GATT Article XI:2(c)(i) systematically and furthermore, to identify the invocation requirements for that exceptional provision. Furthermore, the panel also made a significant step in the following: first, the present case showed the effectiveness of the GATT substantial rules even as regards agricultural trade in which the GATT had been undermined, by providing a detailed interpretation of the exceptional clause under Article XI:2(c)(i);¹⁰⁰ second, the case demonstrated that the GATT dispute settlement procedure could function effectively in order to settle a dispute even on agricultural products which concerned measures exerting a serious influence on domestic politics.

In actual fact, the Panel was able to expose problems and limitations in the provision. The invocation requirements for the exceptional provision, i.e. Article XI:2(c)(i), were impractical because any contracting party invoking the provision had to bear in full the burden of proof for its fulfilment of all the requirements of the provision.¹⁰¹ The provision, therefore, did not work well as the exceptional provision for agricultural trade. For example, according to the panel in this case, Japanese import restrictions on dried leguminous vegetable and groundnuts did not meet with the above requirements.¹⁰²

¹⁰⁰This case was followed by four similar cases whose issue was Article XI:2(c)(i) of the GATT, and those cases are: EEC's Restriction on Imports of Dessert Apples (complained by Chile) in **BISD 36S/93 (1990)**; EEC's Restriction on Imports of Dessert Apples (complained by the U.S.) in **BISD 36S/135 (1990)**; Canadian Import Restrictions on Ice Cream and Yoghurt in **BISD 36S/68 (1990)**; Thailand's Restriction on Importation of and Internal Taxes on Cigarettes in **BISD 37S/200 (1991)**.

¹⁰¹To illustrate the extreme difficulty anticipated by contracting parties invoking this provision, none of the four cases mentioned (see those cases, *ibid.*) has succeeded in fulfilling of all those requirements.

¹⁰²**BISD 35S/163**, *supra* note 90, para. 6.9, at 245.

In the meantime, the participants of the UR reached the Agricultural Agreement in December 1993.¹⁰³ With respect to agricultural products, since the attainment of the Agricultural Agreement, it can be recognised that the exceptional provision of GATT Article XI:2(c)(i) loses its substance which eventually leads to a substantial solution of the problematic issues of this provision.¹⁰⁴ The case, therefore, was not only a leading case involving agricultural trade but also an aid to the cohesion of the principle of liberalisation in agricultural trade which was a product of the Agricultural Agreement of the UR.

In addition, the following may also be noted:

1. With respect to Japan as a "Respondent"

i) Why did Japan insist on the same reason that had been made in the preceding case between the EC and Hong Kong,¹⁰⁵ as one of the arguments in justifying its import restrictions? In this preceding case, the GATT panel clearly stated that "social and policy considerations were irrelevant where they conflicted with GATT legal provisions".¹⁰⁶ Furthermore, having experienced the Leather case in 1983, for example, one could speculate that Japan's argument in referring to "social and policy considerations" in the present case was perhaps really because of other reasons, namely, the domestic necessity to improve the national industry in question and/or the lack of co-ordination among ministries in charge of the preceding and the present cases.¹⁰⁷

¹⁰³Agreement on Agriculture, Final Act Embodying The Results Of The Uruguay Round of Multilateral Trade Negotiations (hereinafter "the Agricultural Agreement"), Marrakesh, 15 April 1994.

¹⁰⁴According to Article 2 (Product Coverage) and Annex 1 to the Agricultural Agreement, this Agreement does not apply to fishery products, which means that the provision of Article XI:2(c)(i) of the GATT remains effective.

¹⁰⁵Report of panel on EC quantitative restrictions against imports of certain products from Hong Kong, **BISD 30S/129 (1984)**, *supra* note 26, para. 28; with regard to the present agricultural case, **BISD 36S/163 (1989)**, para. 5.4.1.4.; also in Report of panel on Japanese measures on imports of leather, **BISD 31S/94**, *supra* note 4, para. 44; and in Report of panel on Japanese customs duties, taxes and labelling practices on imported wines and alcoholic beverages, **BISD 34S/83 (1988)**, *supra* note 47, para. 5.13:

¹⁰⁶*Ibid.*, **BISD 30S/129**, para. 28.

¹⁰⁷For instance, the MITI was responsible for the Leather case, while the MAFF and MOFA were in charge of the Agriculture case; for the issue of lack of co-ordination, see, *infra* note 113.

ii) It seems that the GATT dispute settlement procedure has been shifting from a "pragmatic approach" (or "non-legalistic approach"), which mainly concentrating on negotiations and conciliations, towards a "legalistic approach" with more emphasis on impartial rules as happens in adjudication. In this case, the GATT panel demonstrated a more legalistic approach by applying the provisions of the GATT strictly to the agricultural trade in which the GATT had been conducting its pragmatic approach in settling the dispute at issue for a long period.¹⁰⁸ Whereas, as explained, the stance taken by Japan toward this case was still based on a pragmatic approach, although it was more legalistic than in previous cases to which Japan was a party.

2. With respect to the panel

There are some points on which the panel took a legalistic approach in this case on the one hand, but also approached pragmatically on the other:

i) The panel did not merely examine the issue of legal consistency with the GATT rules but also provided the party concerned with guidance concerning the measures to be adjusted in order to resolve the issues in dispute. For example, despite the seven criteria to be met in full for invoking the exceptional provisions of Article XI:2(c)(i), the panel actually did make a decision based on the fulfilment of some of those seven requirements.¹⁰⁹ Perhaps, this shows that the panel's decision in this case was made not only legalistically but also pragmatically.

¹⁰⁸This legalistic approach taken by the GATT in this case would be evident in aspects as follows: its strict interpretation of Article XI:2(c)(i) of the GATT; its stance of no consideration of the other countries' practices; its exclusion of the uniqueness of Japanese agriculture, Japan alleged as "other pertinent elements" BISD 35S/163, *supra* note 90, paras. 5.4.1-5.4.1.5., at 240-242, in an attempt at settlement of disputing issue; the existence of ongoing negotiations at the Uruguay Round.

¹⁰⁹For instance, concerning Miscellaneous Import Quotas of Japan, in spite of the failure to meet with the requirements designated for the categorised import quotas, the panel continued its judgement to cover the case whether any other requirement were fulfilled if the Miscellaneous Import System was abolished because of minor changes in its administration.

ii) Are there discrepancies in the rulings made by the panel?:

(a) The panel concluded that Japan was unable to provide evidence for its import restrictions on dried leguminous vegetable and on groundnuts. Nevertheless, the panel further concluded that "these two particular products are otherwise justified under the provision of Article XI:2(c)(i)".¹¹⁰

(b) The panel stated that "those import restrictions on the other ten products are not justified under the exceptional provisions of Article XI:2(c)(i)".¹¹¹

Judging from the two rulings indicated, one might infer that the panel made a definite ruling as to ten agricultural items and indefinite rulings as for other two agricultural items. One could, therefore, assume that the panel combined a pragmatic and legalistic approach in arriving at a decision in this case.

iii) The panel examined the propriety of the exceptional provisions under Article XI:2(c)(i) which had not been invoked by the parties to the dispute. For example, the panel ruled Article XI:1 to be also applicable to import monopolies. This panel decision, therefore, brought into question the propriety of invocation of exceptions under Article XI:2(c)(i). Subsequently, the panel carried out its examination whether the items subject to an import quota through an import monopoly and related items fulfilled the requirements for the exceptional invocation under Article XI:2(c)(i). As a result, the panel denied the possibility of the matter on the ground that Japan had not met with the burden of proof as required. Nonetheless, Japan primarily had asserted inapplicability of Article XI to import restrictions by means of an import monopoly.¹¹²

To sum up, albeit this case left a number of questions unanswered in terms of the Panel's examination, especially with respect to the area of agricultural trade, it had made an impact in strengthening the liberalisation of agricultural trade which finally

¹¹⁰BISD 35S/163, *supra* note 90, para. 6.9, at 245.

¹¹¹*Ibid.*, paras 6.5-6.8, at 244-5.

¹¹²In fact, Japan had not invoked the exceptional provisions under Article XI:2(c)(i) of the GATT, at least, as far as prepared and preserved beef products are concerned.

materialised in the Agricultural Agreement at the UR. Overall, since the Panel tried to approach the issues more legalistically, this case could be recognised as one of the leading cases dealing with the contentious issue of agricultural trade. While, Japan's approach at the panel proceedings left questions unanswered. As mentioned, Japan repeated the same arguments which were used unsuccessfully in the Leather case of 1983. This, as explained earlier, might have occurred because of the fact that different Ministries were in charge in the respective cases, which may have led to a lack of co-ordination.¹¹³ Furthermore, defeat in the present case influenced substantially Japan's strategy in succeeding cases, in particular, the Beef and Citrus case ('88) and the Semiconductor Retaliation dispute ('87), which will be examined later. Thus, the present case became important in the dispute settlement history of Japan, and therefore should be regarded as one of the essential cases in our case studies.

7.1.1.4. The Semiconductor Case - Restrictions on Semiconductors (European Community v. Japan)¹¹⁴

Summary of Facts and Procedure:

Since the 1980's, the United States, the largest producer and also exporter of semi-conductors, had been replaced by Japan in terms of exports. Under such circumstances, the semi-conductor industry in the U.S. was concerned about the Japanese closed-market and also about the unfair trade practices conducted by Japanese companies in the U.S. While an anti-dumping investigation was being conducted by the U.S. Commerce Department (DOC), on 14 June 1985, the United States Semi-conductor Industry Association (SIA) filed a petition against Japan under Section 301 of the Trade Act of 1974. As a result of long-running negotiations between Japan and the U. S., the Arrangement concerning Trade in Semi-conductor

¹¹³See, *supra* note 107 and *infra* notes 133 and 138.

¹¹⁴ Complaint was made on 20 February 1987 (L/6129); Japan - Trade in Semi-Conductors, L/6309 (24 March 1988), in *BISD 35S/116-63 (1988)* (4 May 1988); for the summary of this case can be found in, Hudec, *The Enforcing*, *supra* note 2, pp. 541-542, in Pescatore, *The Handbook*, *supra* note 2, pp. CS68/1-/3; and in Matsushita, Mitsuo., *International Trade and Competition Law in Japan*, Oxford University Press, Oxford, 1993, pp. 237-241.

Products (hereinafter, the "Arrangement") was signed on 2 September 1986.¹¹⁵

After concluding the Arrangement between Japan and the U. S., on 20 February 1987,¹¹⁶ the EC filed a complaint that Japanese measures were contrary to the GATT's prohibition on quantitative restrictions under Article XI. The primary focus of the panel was on a prohibition on quantitative restrictions so provided for in Article XI and also its application to this particular case. The panel also analysed the nature of the monitoring procedure for third country dumping by the EC. In response to the questions raised by the EC, Japan merely responded that its measures practised by the government were "non-legally-binding" administrative guidance. Semi-conductor exports and production were limited by the business decisions of private companies.

According to the Arrangement, Japan would monitor the cost and export prices of semiconductors exported by Japanese producers to overseas markets. These

¹¹⁵Japan-U.S. Arrangement Concerning Trade in Semiconductor Products, 2 September 1986, reprinted in 25 I.L.M. 1409 (1986); the following is an overview of the Arrangement which consists of three sections:

The first section refers to market access, which provides that: (i) the Japanese government will make efforts to encourage the sales of semi-conductors produced by foreign manufacturers in Japan through the establishment of an organisation which provides various assistances to those foreign manufacturers; (ii) the government of the U.S. will strengthen its promotion of sale for the U.S. semi-conductor manufacturers; (iii) there should be full and equitable access available for foreign companies to patents resulting from government-sponsored research and development; (iv) both governments should refrain from policies or programmes which motivate inordinate increases in the capacity of semi-conductor production. (BISD 35S/116, para 13)

The second section dealt with prevention of dumping in the following three sub-sections; the first one mentions the suspension of all present anti-dumping cases; the second one stated that the Japanese government will monitor costs and prices on semi-conductor products exported to the U. S. and that if any monitored product is being sold or exported at prices lower than the company-specific fair value, the U.S. government may request consultations immediately, and based on monitoring and/or consultation, the Japanese government will prevent such exports to the U. S. and other significant market by taking appropriate actions available under Japanese laws and regulations; and, the last one deals with the monitoring costs and export prices on the products exported by Japanese semi-conductor manufacturers to significant markets. (*Ibid.*, para. 14)

The third section refers to general provisions on the following matters: periodic and emergency consultations; the conditions for amending and terminating the Arrangement; a provision of being in conformity to rights and obligations under the GATT; and the duration of the Arrangement for five years ending on 31 July 1991. (*Ibid.*, para. 15)

¹¹⁶L/6129, *supra* note 114.

arrangements were made possible by the Japanese government through the introduction of an "administrative guidance" (or "*gyoseishido*" in Japanese).¹¹⁷ The Japanese government took the measures to implement the Arrangement.¹¹⁸

¹¹⁷For detail explanation of "administrative guidance" ("*Gyoseishido*") in Japan, see Matsushita, Mitsuo., International Trade and Competition Law in Japan, Oxford University Press, Oxford, 1993, pp. 59-73; Harley, John O., "Administrative Guidance versus Formal Regulation: Resolving the Paradox of Industrial Policy", in Law and Trade Issues of the Japanese Economy, Saxonhouse, Gary R. & Kozo Yamamura eds., University of Washington Press, Seattle, 1986, pp. 107-128.

¹¹⁸Implementation of the Arrangement by Japan:

(a) Access to the Japanese market (BISD 35S/116, paras. 17 and 18)

The Japanese government requested Japanese major users or purchasers of semi-conductors to co-operate in increasing the purchase of foreign-based products, also the MITI organised meetings with the top ten major users of the products in order to make the same request. In addition, in March 1987, the International Semi-conductor Co-operation Centre was established and whose main purpose was to promote the sales of foreign semi-conductors.

(b) Monitoring (*Ibid.*, paras. 20, 21 and 23)

With respect to the monitoring of the export prices of semi-conductors, i.e. the Director-General of the Machinery and Information Industries Bureau and the Minister of MITI, organised meetings with producers and exporters in order to request that dumping should be avoided. Nonetheless, these requests were not legally binding but simply a form of general appeal.

The system of export approval for semi-conductors, based on the Foreign Exchange and Foreign Trade Control Law, was introduced in order to enforce COCOM.* In addition, this system had been utilised to monitor export prices of semi-conductors since November 1986. The threshold for shipments of semi-conductors which required export licences was reduced from one million to five hundred thousand Japanese yen in January 1987. As a result of this change, the number of applications almost doubled, thus causing delay in the processing of certain licence applications. In addition to the above factor, in some cases, incomplete information in applications also caused delay. There was no time limit, whether maximum or minimum, for processing export licence applications. The time taken to process licence applications varied from a couple of weeks to several months depending on factors relating to each case.

*COCOM (Co-ordinating Committee for Export Control) is a voluntary group, whose headquarters was inside the U.S. Embassy in Paris, and which was set up by the Western alliance (most of NATO nations) for the purpose of export controls over strategic goods bound to the Communist Areas such as the former USSR, China and Eastern European countries. Its role, however, has been diminished in recent years.

The procedures for the price data collection were established in accordance with Article 67 of the Foreign Exchange and Foreign Trade Control Law, and Article 10 of the Export Trade Control Order. In cases of failure to report or submission of false reports were liable to a penalty like servitude not exceeding six months or a fine not exceeding two hundred thousand Japanese yen. Non-compliance in this regard, however, would not lead to the denial of export licence or prohibition of exportation. In case the MITI found cases in which export prices were "extremely below costs", it would inform such companies of the facts and of MITI's concern. The MITI did not decide minimum export prices and MITI's communication to the company were not bound by law. Companies were, therefore, expected to understand that it was their own self-interest to deter dumping, and to take action accordingly. The MITI did not take the existence or non-existence of injury in foreign importing countries into consideration, when watching costs and export prices. The revised Foreign Exchange and Foreign Trade Control Laws, effective from 10 November 1987, which strengthened the regulations on reporting COCOM-related commodities had separated

The details of the legal claim expressed by the EC were:

(1) With respect to export restrictions:

-In spite of the lack of legal compulsion, the procedure for monitoring exports to discourage exports at dumping prices established that an export restriction was in violation of GATT Article XI:1; (Paras. 49, 51)

-Export restriction on dumped exports also constituted violation of GATT Article VI, on grounds that this Article provides importing countries with sole right to accept or prevent dumping; (Paras. 43, 47)

-Delays in obtaining an "automatic" export permission were also considered to be an export restriction, which consisted of a violation of GATT Article XI:1;

-The failure to apply an export restriction to the smallest export markets, violated both the MFN obligation stipulated in GATT Article I:1 (Article XIII alternatively) (Para. 56) and the obligation of "commercial considerations" under GATT Article XVII:1(c); (Para. 58)

-Whether a violation or not, Japanese measures to increase export prices of important industrial component established a Non-Violation of Nullification & Impairment of basic benefits of trade liberalisation under GATT. (Para. 69)

(2) With respect to import access:

-Japanese measures to improve access to Japanese market were in favour of U. S. imports, which violated the MFN obligation under GATT Article I:1. (Paras. 60, 61, 63)

export approval from monitoring as far as semi-conductors were concerned.

In addition to the above two main measures, i.e. the export monitoring and import access, Japan's measures lacked transparency, thus violating GATT Article X. (Para. 64)

In response to those assertion by the EC, the Japanese government argued:

(1) With respect to alleged violation of Article VI:

In Article VI, there was no specific provisions to prohibit actions taken to prevent dumping by exporting countries. On the contrary, anti-dumping actions conducted by exporting countries were in accordance with the spirit of the GATT. (Para. 45)

(2) With respect to alleged violation of Article XI:

The monitoring of semi-conductor exports by the Japanese government was simply for the purpose of checking cost and export prices. Furthermore, such monitoring was not intended to prohibit or restrict trade, nor did it in practice result in such. Through monitoring, Japanese companies were encouraged by the Japanese government to prevent dumping, although this encouragement was not legally binding by any means. In fact, the companies were expected to refrain from dumping of their own will. Therefore, such voluntary actions of the companies were irrelevant to the provisions of Article XI which stipulated government action. (Para. 50)

In the present case, besides the disputing parties, the U. S.¹¹⁹ and five other interested countries (Australia,¹²⁰ Canada,¹²¹ Hong Kong,¹²² Singapore,¹²³ and Brazil¹²⁴) submitted individual arguments to the Panel. This is an example of a case which involves the issue of "co-defendants". Furthermore, in the case of disputes concerning "grey area" measures¹²⁵ involving two countries, a complainant normally

¹¹⁹For arguments submitted by the U. S., see **BISD 35S/116**, *supra* note 114, paras. 72-82.

¹²⁰For Australia's arguments, see *ibid.*, paras. 84-86.

¹²¹For Canada's arguments, see *ibid.*, paras. 87-89.

¹²²For Hong Kong's arguments, see *ibid.*, paras. 90-92.

¹²³For Singapore's arguments, see *ibid.*, paras. 93-94.

¹²⁴For Brazil's arguments, see *ibid.*, para. 95.

¹²⁵The legality of this trade actions is not clearly addressed in the GATT rules. Those actions, for instance, include Voluntary Export Restraint Agreements (VRAs) and Orderly Marketing Agreements (OMAs). The issue of grey-area measures closely links with "safeguards" issue (see, for example, GATT Article XIX, XII, XVIII); cf. Under the

makes a complaint against one of the countries which is required to introduce such measures due to its weaker position in a political scene between them. A country (the U.S.), which requested the other country (Japan) to adopt such measures, can only participate in a case as a third party at a panel procedure, which remains the case under WTO.¹²⁶

Summary of Findings and Conclusions:

Finally, in 1988, the panel arrived at a decision: Article XI:1 applied broadly to any measures including non-mandatory governmental measures that had similar effects; the panel examined measures not just as regards its legal status but as to the substance of the Japanese government's action; the monitoring procedure, although non-legal-binding administrative guidance, met with criteria being whether the measures created incentives for the relevant businesses to observe restrictive policies and also whether the measure was necessary for the efficacious implementation of a restrictive policy; national measures adopted in order to prevent dumping did not justify export restrictions contrary to Article XI:1; Article VI did not prohibit actions taken by exporting countries to restrict dumping; excessive delays such as up to three months in issuing exporting licences resulting from the system of monitoring of costs and export prices of semi-conductors were thus in contravention of Article XI:1; Japanese measures concerning restrictions of semi-conductors exports to overseas markets were found to be inconsistent with Article XI:1, and were considered to have nullified and impaired benefits accruing to the EC under the GATT. Furthermore, the panel also referred to the 1987 panel decision of administrative guidance concerning a Japanese agricultural import restriction.¹²⁷

Agreement on Safeguards Article 11(b), the "grey area" measures are prohibited.

¹²⁶Cf. Article 4.11 of the DSU (Joint Consultation); for example, see *India v. Turkey* dispute over Turkey's restrictions on imports of textile and clothing products (WT/DS34). Earlier, India had requested to be joined in the consultation between Hong Kong and Turkey on the same subject matter (WT/DS29). Hong Kong reserved its third-party rights along with four other member states at the DSB meeting on 13 March 1998 when it established a panel.

¹²⁷See *BISD 35S/163*, *supra* note 90.

As a result, Japan was required to alter its monitoring system concerning the export and sale of semi-conductors in conformity with the requirements of the GATT. In 1989, the Japanese government changed the monitoring system so as to meet the requirements of the panel report.¹²⁸ In 1990, Japan and the EC reached an agreement by which Japan agreed to sustain minimum export prices on semi-conductors for the EC market.¹²⁹

Remarks on the case:

In the case of ordinary VRA, exporting countries merely restrain export prices and export volume of products for their counterparts, whereas in the case of the Arrangement (between Japan and the U.S.) at issue, the provisions provided for an increase in the market share of semi-conductors originating in foreign countries in the Japanese market, and also for restrictions to the export prices of semi-conductors destined for third countries. Needless to say, many countries demonstrated great concern over the present case concerning the Arrangement between Japan and the U. S. and many of them, in fact, reserved the right to make submissions to the Panel. In the following, two main findings with respect to Article XI:1 and Article VI:1 in the Panel report are analysed:

(1) With respect to GATT Article XI:1

In the Panel report, there are three points to be noted in terms of Article XI:1. First, the issue of whether prevention of exports below specific prices would constitute "prohibitions or restrictions" of exportation under Article XI:1. Second, the issue whether the measures taken should be legally mandatory. The last point is that if the measures are non-mandatory, what sort of non-mandatory measure would be

¹²⁸For commentary on this case, Amelia Porges, (International Decisions) "GATT Dispute Settlement Panel", 83 Am. J. Int'l. L. (1989) pp. 388-394; Prendergast, James W., "The European Economic Community's Challenge to the U. S. - Japan Semiconductor Arrangement", 19 Law & Pol'y Int'l Bus (1987), pp. 579-601; Kingery, John C., "The U. S. - Japan Semiconductor Arrangement and the GATT: Operating in a Legal Vacuum", 25 Stan. J. Int'l L. (1989), pp. 467-497; for relevant study see Long, William J., "The U. S. - Japan Semiconductor Dispute: Implication for U. S. Trade Policy", 13 Md. J. Int'l L & Trade (1988), pp. 1-37.

¹²⁹Commission Regulation (EEC) 165/90 (23 January 1990) OJ. No. L20/5. (Export restraints involved in antidumping settlements are implicitly authorised by MTN Antidumping Code.)

regarded as measures within the definition of Article XI:1? Further analyses regarding each item follows:

i) In making its finding with respect to the first issue, the Panel did not differentiate import and export restrictions. The Panel referred to a previous case¹³⁰ whereby the import of a product priced below a minimum price level constituted a restriction on importation within the meaning of Article XI:1. The Panel then applied the same standards to restriction on exports below certain prices. According to the same principle established by the Panel, this norm could apply to the restraint of export volume, and perhaps the ordinary VER could be prohibited because of its inconsistency with Article XI:1.

ii) As mentioned earlier, the Panel confirmed that Article XI:1 would apply to any measures which restricted exports, regardless of the legal status of the measures. According to the Panel, Article XI:1, unlike other provisions of the GATT, did not refer to law or regulation but to measures in a broader sense.¹³¹ Accordingly, the Panel concluded that systematic monitoring along with the utilisation of supply and demand forecasts constituted a coherent system what restricted the sale for export of semi-conductors at prices below specified cost to the company, inconsistent with Article XI:1.¹³² Judging from the wording and the objectives of this Article, it seemed reasonable that the Panel made its conclusion with emphasis on the actual effect of the measures at issue.

Furthermore, the Panel referred to a precedent which may be of extra assistance in examining the measures at issue. The case¹³³ cited by the Panel related to restrictions on imports of certain agricultural products maintained by the Japanese government. With respect to this citation, it is interesting to note that, unlike an ordinary citation that merely refers to the gist and source of the case, a detailed reference was made consequently, to the arguments between the complaining party and Japan. Then, the

¹³⁰See, EEC - Programme of Minimum Import Prices, Licences and Surety Deposit for Certain Processed Fruit and Vegetables in **BISD 25S/99**.

¹³¹**BISD 35S/116**, *supra* note 114, para 106.

¹³²*Ibid.*, para. 132, A.

¹³³Japan - Restriction on Imports of Certain Agricultural Products (**L/6253**) in **BISD 35S/163**, *supra* note 90.

Panel supported Japan's contention and concluded that the "administrative guidance" in the special circumstances prevailing in Japan could be regarded as "governmental measures" enforcing supply restriction.¹³⁴ Here, it is worth noting that the panel procedure of the Agricultural Products case coincided with the present Panel, the Panel report on the former¹³⁵ being adopted just before the adoption of the latter case.¹³⁶ Presumably, such an exceptionally detailed reference to another panel report might have been made because of the fact that contradictory arguments¹³⁷ were made by the Japanese government on the same issue (i.e. the legal nature of "administrative guidance") in the two different Panel proceedings. Did that contradiction have any impact on this Panel decision? Whether the answer is "yes" or "no", one finds it necessary to explain the Japanese strategy at the panel proceedings. One possible reason might be that there had been a lack of co-ordination in the Japanese government due to an inter-ministerial rivalry.¹³⁸ On this assumption, the Ministry of Agriculture, Forestry and Fisheries (MAFF) in consultation with the Ministry of Foreign Affairs (MOFA) was in charge of the Agricultural products case; while the MITI, normally acting independently in dealing with disputes, was in charge of the present case. This could be one of the reasons why Japan made such contradictory arguments at the two different panel proceedings, which is less than ideal in terms of strategy.

iii) With respect to the third point, i.e. the Panel requested that two criteria be met in order that non-mandatory measures be regarded as measures within the meaning of Article XI:1. Those essential criteria were: (1) there were reasonable grounds to believe that sufficient incentives or disincentives existed for non-mandatory measures to go into effect; (2) the operation of the measures to restrict export of

¹³⁴BISD 35S/116, *supra* note 114, para. 107

¹³⁵2 February 1988 (C/M/217).

¹³⁶4 May 1988 (C/M/220).

¹³⁷See, the two different explanation for governmental measures (i.e. "administrative guidance") in Japanese contention: for "Non-binding" one, *ibid.*, paras. 50, 54, 107 and 109; for the "Binding" one, BISD 35S/163, *supra* note 90, paras. 3.2.6. and 5.2.2.2.

¹³⁸See, Matsushita, Mitsuo., and Thomas Schoenbaum, Japanese International Trade and Investment, Tokyo University Press, Tokyo, 1989 at pp. 24-25 in Jackson, John H., W. J. Davey and Alan O. Sykes, Jr., Legal Problems of International Economic Relations [hereinafter, the "Int'l Econ. Relations"], 3rd ed., West Publishing Co., St. Paul, Minnesota, 1995 at 222; cf. the Agriculture case at Section 7.1..1.3. of the thesis.

semi-conductors was essentially dependent on action or intervention of the government.¹³⁹

With regard to criterion (1), the Panel considered that this criterion was satisfied by circumstances¹⁴⁰ such as, the negotiation process between Japan and the U.S. and the Japanese policy statement then made. The Panel, however, considered that these circumstances were, of themselves, insufficient to ensure compliance.¹⁴¹ Therefore, further governmental measures were required to ensure compliance.

The Panel then moved on to consider criterion (2) and concluded, based on all the factors¹⁴² (e.g. the Japanese government's own description of its measures as provided to the U.S. in its Position Paper of April 1987, the structure and elements of the measures adopted by the Japanese government, the operation of the supply and demand forecast compiled by the Japanese government) that an administrative structure had been created by the Japanese government which operated to exert maximum pressure on the private sector to cease exporting at below costs specified by a company.¹⁴³ In the process of confirming the existence of the second criterion, what was important was that the Panel took considerable much account of a series of concerted actions and measures taken by the Japanese government. Although the Japanese government repeated its contention as to its consistency with Article XI:1 and its intention to prevent dumping; no Japanese measures were in fact restrictions under Article XI:1 due to their failure to be legal binding or mandatory. The export restraint of semi-conductors below company-specific cost was initiated by the companies through a voluntary decision. It, therefore, would not make sense to discuss each action or measure taken by the Japanese government, because it was obvious that the Japanese government intended to restrict the export of semi-conductors destined for third countries to below company-specific cost and furthermore, the same objectives were shared by a series of actions and measures taken by the Japanese government.

¹³⁹*Ibid.*, para. 109.

¹⁴⁰*Ibid.*, para. 110.

¹⁴¹*Ibid.*, para. 111.

¹⁴²*Ibid.*, paras. 112-114.

¹⁴³*Ibid.*, para 117.

Besides the above explanation for conformity with criterion (2), the "administrative guidance" of Japan should be mentioned briefly. It is essential to identify the nature of Japanese administrative guidance and to ascertain whether it applied to "other measures" under Article XI:1. In general, the Japanese administrative guidance was understood to be guidance, recommendation, or non-legal by binding advice. Exceptionally, administrative guidance of a mandatory nature can be also noted amongst the rights available to the competent governmental authorities to accomplish their administrative policy objectives. For example, the Automobile Voluntary Export Restriction to the United States¹⁴⁴ was clarified by the MITI to be a restriction that was, in practice, as a whole a mandatory measure despite the fact that the company-specific volume of exports was decided by administrative guidance. In cases where the guidance was not complied with, the MITI could consider invoking mandatory action under the Export Trade Control Order. Additionally, as mentioned above, non-mandatory administrative guidances can be recognised, for instance, in guidance for the establishment of a trade association.

An administrative guidance in Japan is still an effective and important policy tool for the Japanese government although its effectiveness has decreased to a certain degree, compared with previous decades, and in this respect, a few factors¹⁴⁵ could be given response to the question:

First of all, the wide usage of "administrative guidance"¹⁴⁶ in Japan is explicable because it is supported by the extensive authority of administrative approval reserved to the governmental authorities. Secondly, the wide scope of powers retained by the governmental authorities and broad discretion of the Japanese courts in choosing to

¹⁴⁴For further explanation, see in Matsushita, M., *supra* note 114, pp. 235-6; A number of important trade issues raised between Japan and other major trading countries have been resolved through Voluntary Export Restraints (VERs) despite criticisms against them, and in that sense, they played an important role in settling trade disputes before reaching to GATT; for the purpose of VERs in the case of Japan, there are mainly two reasons, see, *infra* note 149.

¹⁴⁵See the observation on administrative guidance by Professor Matsushita, *ibid.*, pp. 67-69.

¹⁴⁶The definition of "administrative guidance" was expanded in the recent Panel report on Japan - Measures Affecting Consumer Photographic Film and Paper [hereinafter, the "Japan Film"], WT/DS44/R (31 March 1998), paras. 6.92-6.96 and 10.43-10.56; read in general Section 8.1.2.2. of this thesis.

grant approval, ensured a strong incentive for those who received such administrative guidance to abide by it. Thirdly, the attitude of the Japanese business community, in general, is to welcome, with a degree of obedience or submissiveness, administrative guidance constructively. Such a positive stance taken by the Japanese companies is necessary because of benefits provided by the administrative guidance such as, control over excessive competition, maintenance of order within the industrial community, and evasion of responsibility, etc. Finally, in the case of trade conflicts with other countries, it is essential for Japanese companies to have assistance from the Japanese government. For example, if a Japanese company, which was unduly discriminated against in another country, wants to pursue this foreign country under the GATT rules, it needs to seek the involvement of the Japanese government and request appropriate actions accordingly (i.e. diplomatic protection applies in case of international trade dispute under the GATT/WTO system).

It is therefore important for the Japanese business community to maintain a sound relationship with the Japanese government. In addition, successful accomplishment of administrative objectives set by the Japanese government have been achieved through mutual respect and positive co-operation between the Japanese government and business community. Further, in Japan, the effectiveness and efficiency of administrative guidance has been established and has been functioning well. Hence, Japanese administrative guidance could be reasonably deemed as an illustration of restriction through "other measures" stipulated in Article XI:1 at issue.

(2) With respect to GATT Article VI:1

The Panel found that Article VI did not provide a justification for measures restricting the exportation or sale for export of a product which was inconsistent with Article XI:1.¹⁴⁷ The EC's contention was that the Article VI provision gave an exclusive right of preventing dumping to importing countries. The Panel, however, noted that Article VI provided importing countries with the right to levy anti-dumping duties subject to specific conditions.¹⁴⁸ Here, it may be noted that the

¹⁴⁷BISD 35S/116, *supra* note 114.

Panel did not refer to the actions taken by the exporting country. It might be the case that the Panel have intentionally avoided giving a precise finding on this point at issue.

As the Panel already noted, the only permissible anti-dumping measures provided for in Article VI is to levy anti-dumping duties in specific conditions subject to consistency with Article XI:1. Accordingly, no countries, whether importing countries or exporting, can take any actions if these are inconsistent with Article XI:1. Therefore, one could assume, based on the fact that no actions by exporting countries are mentioned under Article VI, that it may be reasonable to draw a conclusion that any actions taken by exporting countries that would be inconsistent with other provisions of the GATT could not be justified by Article VI, even if such actions were taken for antidumping purposes. In addition, this conclusion could be reflected in the provision of Article VI:1 whereby "*...the dumping, ..., is to be condemned if it causes or threatens material injury to an established industry in the territory of a contracting party or materially retards the establishment of a domestic industry*". Furthermore, the GATT defined anti-dumping action as a measure of 'exception' and 'remedy' and it also, in principle, gave priority to examining the abuse of the right to levy anti-dumping duties. Accordingly, it would be difficult to interpret this provision so as to extend the right of taking an anti-dumping action to exporting countries (Japan in the present case).¹⁴⁹

To sum up, there are three significant points to be noted in this Panel report. These points are: 1) whether the bilateral agreement of voluntary restriction on exports establishes a breach of provision of GATT Article XI; 2) whether an administrative guidance (non-legal binding) is inconsistent with the provision of GATT Article

¹⁴⁸*Ibid.*, para 121.

¹⁴⁹The justification of VERs made by Japan were based upon two points: (i) the prevention of Anti-Dumping measures; (ii) the avoidance of unilateral measures (mainly the U.S. Section 301), which were reiterated even in the first report on Japan after the present panel, see the Council Minutes of Meeting on Trade Policy Review Mechanism: Japan, C/RM/M/8 (8 October 1990), Section II. Introductory Remarks by the Representative of Japan, paras. 16,17 and 145; Note that regarding Japan's justification of VERs listed above under (ii), one should recall the consistent line in Japanese submission to the UR negotiations on DS, i.e. Japan insisted upon the prohibition of unilateral actions (mainly targeted the US Section 301) and finally its strong request (along with the EC's and others) became Article 23 of the DSU.

XI:1; and 3) the nature of GATT Article VI - differences appeared between Japan and the U. S. on one hand and the EC on the other. The followings are comments for each of the aspects listed in the Panel report:

1) The most significant matter dealt with in this Panel report was the question of whether the bilateral agreement of voluntary restriction on exports constituted a contravention of the provision of Article XI.¹⁵⁰ The Panel found that the voluntary restriction on the export of products, in particular, the one destined for third countries was in violation of the GATT. It is more unlikely to find a disputing issue concerning the VER between the signatories of the bilateral agreement. Nonetheless, in this Panel report, the Panel indicated that the same grounds for its finding could also be applied to the voluntary restriction on trade between the signatories of the bilateral agreement. It would therefore be noteworthy to recognise that if the voluntary restriction under the bilateral agreement involved third countries' interests, a violation of the GATT would be constituted by the voluntary restriction. It should be mentioned that the GATT legality of voluntary restrictions (also of other variations such as export restrains, agreement, and arrangement) has been discussed in the last few decades within the GATT framework. Recently, in particular, the UR negotiations has achieved some significant progress to regulate the actions through voluntary restrictions ("grey-area measures" in general), which can be found in the WTO Agreement on Safeguards.¹⁵¹

¹⁵⁰"Under the GATT obligations, many and probably most of the so-called export restraint arrangements are more than likely inconsistent with the obligations of GATT" in Jackson, J., The World Trading System [hereinafter, the "Trading System - 2"], 2nd ed., The MIT Press, Massachusetts, 1997, at 205.

¹⁵¹For example, Article 11.1(b) of the Agreement on Safeguards stipulates "Prohibition and Elimination of Certain Measures", which states "...a Member shall not seek, take or maintain any voluntary export restraints, orderly marketing arrangements or any other similar measures on the export or the import side". The WTO Agreement, therefore, prohibits the grey-area measures; see also Article 11.2 which prescribes the timetable for phasing out of those special measure as referred to in the para. 1(b) above: "...all measures ... to be phased out or brought into conformity with the [Agreement on Safeguards] within ...four years after the date of entry into force of the WTO Agreement". Nevertheless, one exception is allowed for each importing member, which must be mutually agreed between members concerned and notified to the Committee on Safeguards within 90 days of the entry into force of the WTO Agreement. This exception, to which the EC is entitled until 31 December 1999 [the "commercial consensus"* on passengers cars, off road vehicles, light commercial vehicles, light trucks (up to 5 tonnes), and the same vehicles in wholly knocked-down form (CKD

2) Concerning the second point, the Panel also make it clear that non-legal binding action such as "administrative guidance", under certain circumstances, could be inconsistent with the provision of Article XI:1.¹⁵² The main issue here was whether the actions taken by the Japanese government to implement the Arrangement signed between Japan and the U. S. contravened "restrictions on the exportation or sale for export" stipulated in Article XI.¹⁵³ As one can note from the wording "... the Panel noted that Article XI:1..., did not refer to laws or regulations but more broadly to measures"¹⁵⁴ in the Panel report, the Panel emphasised the effect of the actions taken by the Japanese government, namely, an "export restriction", rather than the legal status of that action itself. It could, therefore, be reasonable to say that the way the Panel examined the action (i.e. "administrative guidance") taken by the Japanese government was to focus on its "effect". Accordingly, the Panel raised a significant question concerning the significance of administrative guidance to the Japanese government and its importance in enforcing government policies.

3) In the present panel, the EC presented an argument as to the nature of Article VI, which was noteworthy. The EC argued that Article VI did not condemn dumping itself but imposed limits on potential for the taking measures to counteract dumping and subsidisation.¹⁵⁵ However, Japan and the U. S. disagreed with the EC's argument and they contended that, according to the EC, the importing country had the right to purchase a limitless amount of product at low prices, a right which GATT did not ensure.¹⁵⁶ Generally speaking, although the EC's interpretation of Article VI was

sets)] is indicated in the Annex to the Agreement on Safeguards [*The "commercial consensus" was notified to the GATT, see L/6922 (16 October 1991)]; for further reading on this issue, see Jackson, J.H. et al., *Int'l Econ. Relations*, *supra* note 138, Section 13.3, pp. 643ff; Jackson, J.H., *The Trading System-2*, *supra* note 150, Chapter 7, pp. 175-211; Nuzum, Janet A, "The Agreement on Safeguards: U.S. Law Leads Revitalisation of the Escape Clause" in Stewart, Terence P. (ed.), *The World Trade Organisation - The Multilateral Trade Framework For the 21st Century and U.S. Implementing Legislation* [hereinafter, the "WTO"], American Bar Association, Washington, DC, 1996, Chapter Eleven, pp. 407-437; Petersmann, E.-U., "Grey Area Measures and the Rule of Law", 22 J.W.T.L., No.2, (1988), pp. 23-44.

¹⁵²See, *ibid.*, the Japan Film case (WT/DS44/R), *supra* note 146, paras. 6.99 and 10.54 - 10.56.

¹⁵³See **BISD 35S/116**, *supra* note 114, para. 99-116.

¹⁵⁴*Ibid.*, para. 106.

¹⁵⁵*Ibid.*, para. 43.

more commonly accepted, in practice, an individual country takes recourse to anti-dumping measures based on its domestic law which regards dumping as a distortion of trade. Moreover, under such justification, anti-dumping measures work as a substitute safeguard measures. This issue is one of the more contentious issues of the GATT, which has been negotiated at each round but has remained unresolved. It would be useful for Japan as one of the popular targets of anti-dumping proceeding to examine the EC's allegations mentioned above for future cases. Furthermore, with the assistance of the newly established system of WTO, Japan certainly would be able to follow a different policy with legal security as provided for in the WTO Agreement on the issue of trade disputes. Japan, therefore, should not yield as much as previously to political pressure imposed by other countries. Perhaps, through lessons from the present case, Japan might have thought that it should not take a bilateral approach but be multilateral in its approach to settling trade disputes.

To summarise the significance of the present case in terms of Japan's policy on the trade dispute settlement system:

First, not following the conventional pattern, the EC made a claim in the Japan-U.S. Semiconductor Arrangement. Japan, in fact, did not expect such a claim from the EC because, as had happened before, Japan thought that the EC would be silent so long as was offered some concessions.¹⁵⁷ Second, the GATT panel, for the first time, ruled on the issue of VRAs (Voluntary Restraint Arrangements), the prevention of dumping, and finally denied their legality in accordance with GATT rules.¹⁵⁸

Although, Japan was defeated, this bitter experience indeed became an important experience in the history of Japanese dispute settlement of GATT/WTO. The lesson which Japan learnt from this case among others is that the period of "bilateralism" is over. For this reason, one should note the significance of the present case in Japan's DS history of GATT/WTO.

¹⁵⁶*Ibid.*, paras. 71 and 75.

¹⁵⁷An interview with a MITI official, June 1998, Geneva.

¹⁵⁸After the UR negotiations, VRAs and other "grey-area measures" are explicitly prohibited as prescribed in Article 11 on the WTO Agreement on Safeguards; see *supra* note 151.

7.1.1.5. The SPF Case - Imports of Spruce-Pine-Fir (SPF) Dimension Lumber (Canada v. Japan)¹⁵⁹

Summary of Facts and Procedure:

Canada made a complaint against Japan that the products, namely, "Spruce-Pine-Fir (SPF)" dimension lumber, were "like products" to the dimension lumber made from other wood species. Canada alleged that the tariff of 8 per cent on imports of SPF imposed by Japan constituted a violation of equal treatment principle under GATT Article I:1. The main issue in this case was whether the "like product" concept precluded a tariff distinction according to specific wood species. Japan had imported dimension lumber as home construction materials from both Canada and the United States for some time. The key point, however, was that Japan granted a zero tariff on dimension lumber made of hemlock-fir, which was mainly exported from the U. S., whereas Japan imposed an 8 per cent tariff on SPF which came from Canada. The Council finally agreed to establish a panel on 22 March 1988.¹⁶⁰

Canada's arguments:

- A dimension lumber made from SPF and that made from non-SPF are like products under the meaning of Article I:1; the existence of a difference in the application of tariff rates between those two lumbers was inconsistent with MFN under GATT.

- The dimension lumber produced by Canada is mainly SPF (which bears on 8 per cent tariff), whereas the U.S. production is mainly non-SPF dimension lumber (on which is imposed a zero tariff), thus the U.S. was more competitively advantaged in the export of dimension lumber to Japan, and Canada was in a disadvantageous position in the Japanese market; the discriminatory application of the Japanese duty treatment of SPF dimension lumber had brought about a negative impact on Canadian exports.

¹⁵⁹Complaint was made on 18 November 1987 (L/6262).

¹⁶⁰C/M/218 (22 March 1988).

Japan's contention:

-Japan contended that SPF and non-SPF dimension lumber could not be deemed as like products as argued by Canada, and that the different application of tariff duties was not intended to discriminate against Canadian dimension lumber in favour of imports of dimension lumber from other countries.

Summary of Findings and Conclusions:

The Panel considered it essential to identify the GATT principles on tariff structure and classification in order to understand the Canadian complaint. According to the preceding panel, the General Agreement left wide discretion to the contracting parties with regard to the structure of national tariffs and classification of goods within the framework of such structures.¹⁶¹ Since the Japan's adoption of the Harmonised System (hereinafter, the "HS"), a tariff classification going beyond the HS structure was legitimate, as long as such tariff differentiations were not used in such a way that was conducive to discrimination among like products originating in different contracting parties.¹⁶² Then, the Panel stated that the tariffs referred to by the General Agreement were those of the individual contracting parties, therefore it followed that if a claim of likeness was raised by a contracting party in relation to the tariff treatment of its goods on importation by some contracting party, such a claim should be based on the classification used in the importing country's tariff.¹⁶³

The Panel noted in this respect that "dimension lumber" as defined by Canada (i.e. an exporting country) was extraneous to the Japanese Tariff. It was a standard applied by the Canadian industry which appeared to have some equivalents in the U.S. and in Japan itself, but it could not be considered for that reason alone as a category for tariff classification purposes, nor did it belong to any customs classification accepted internationally.¹⁶⁴

¹⁶¹See, the report of the Panel on Tariff Treatment of Unroasted Coffee, **BISD 28S/102** at para. 4.4.

¹⁶²**BISD 36S/167-99**, para. 5.9.

¹⁶³*Ibid.*, para. 5.13.

¹⁶⁴*Ibid.*, para. 5.14.

The Panel, therefore, concluded that reliance by Canada on the concept of dimension lumber was an inappropriate basis for establishing "likeness" of products under GATT Article I:1.¹⁶⁵ The Panel concluded this case by stating that is "...*could not establish that the tariff treatment of Canadian dimension lumber applied by Japan ... was inconsistent with Article I:1 of the General Agreement*",¹⁶⁶ and was in favour of Japan. On 19 July 1989, a Panel report was adopted.¹⁶⁷ In the meantime, Canada announced memorandum which expressed its disagreement with the legal conclusions arrived at by the panel.¹⁶⁸

Remarks on the case:

The present case illustrated the question of definition and interpretation of "like products", which was, a complex issue to deal with. In this case, the Panel did not agree with the concept of "dimension lumber" asserted by Canada, as a category of universal or internationally accepted tariff application, and granted priority to the autonomy and originality of the tariff classification of the importing country (Japan in this case).¹⁶⁹ It is interesting to note that this case became Japan's first as well as only experience of a favourable decision at the GATT Panel despite the fact that Japan had been involved as a respondent under the procedure provided for in GATT Article XXIII:2.¹⁷⁰

¹⁶⁵*Ibid.*

¹⁶⁶*Ibid.*, *supra* note 162, para. 6.1.

¹⁶⁷C/M/235.

¹⁶⁸L/6528 (20 June 1989).

¹⁶⁹*Ibid.*, *supra* note 162, paras. 5.8 and 5.9.

¹⁷⁰This pattern of result (Japan won in a case in which Japan was involved as a respondent) is rare according to the analyses conducted by Professor Hudec, that is, it is more likely to have positive outcomes if a country involves in a dispute as a "Claimant", see Hudec, Robert., *The Enforcing*, *supra* note 2, Chapter 11 (A Statistical Profile of GATT Dispute Settlement Cases: 1948-1989), pp. 273 ff; Note that since the introduction of WTO system, Japan once again experienced its victory, as the same pattern as the SPF case, in Japan Film case (WT/DS44) whose report was adopted by the DSB on 22 April 1998. In addition, there are a few more cases in which Claimant lost a case, for instance: Brazil-Measures Affecting Desiccated Coconut (complained by Philippines) in WT/DS22/R (17 October 1996) and in WT/DS22/AB/R (21 February 1997); EC-Measures Affecting Importation of Certain Poultry Products (complained by Brazil) in WT/DS69/R (12 March 1998); EC-Customs Classification of Certain Computer Equipment (complained by the U.S.) in WT/DS62/AB (circulated to Members on 5 June 1998) which reversed the Panel decision [i.e. the complainant's victory (the U.S.) against the EC]; and Guatemala - Anti-Dumping Investigation Regarding Portland Cement from Mexico, WT/DS60/AB/R (2 November 1998) which also reversed the Panel decision [i.e. the claimant's victory (Mexico) against the

In the panel proceedings, Japan demonstrated two points of significance which should be noted. First, Japan disputed the concept of "like products" based on one of the GATT practices, including the GATT's drafting history (i.e. the fact that it was generally recognised that the term "like products" had different meanings within the different contexts of different articles of the GATT).¹⁷¹ Indeed, contracting parties often referred to the drafting history of GATT at panel proceedings.¹⁷² In this respect, Japan's contention based on the drafting history was reasonable to support its argument under GATT.

Second, Japan made a persuasive contention concerning Canada's view on "tariff sub-classification and the stability of concessions" based on the existing practice of tariff negotiation within the framework of GATT. Namely, Japan argued that what was unacceptable to it was the "sub-classification" of Japan's tariff classification attempted by Canada, and the comparison for likeness of some of the products (i.e. lumber) in different Japan's tariff classifications chosen by the complainant (i.e. the exporting country).¹⁷³ Canada maintained that SPF and non-SPF dimension lumber are like products despite the fact that there was neither a clear definition nor international standardisation of dimension lumber. However, Canada so decided simply by selecting similar elements of these products. According to Canada's contention, the dimension lumber could be made from any species of coniferous trees as finished products with emphases on end-use criteria.

Nonetheless, Japan found this Canadian approach a "compulsory sub-classification". Japan, furthermore, asserted that attempts to determine "likeness" of products in an *a priori* manner, with inadequate consideration to tariff classification, would cause

Guatemala].

¹⁷¹See, the drafting history and interpretation of "like products" in, *ibid.* para. 3.31; "the expression had different meaning in different contexts of the Drafting Charter" in UN-: EPCT/C.II/65 at 2; EPCT/C.II/PV/12 at 7 (1946); EPCT/C.II/36 at 8 (1946); E/CONF.2/C.III/SR.5 at 4 (1947); GATT/CP/4/39 at para. 8; IC/SR. 9 at 2 (1953) and BISD 25S/49-53 and BISD 28S/92-98); the term "like products" can be found in several GATT articles, i.e. I, II, III, VI, IX, XI, XIII and XVI.

¹⁷²For the issue of interpretation of GATT/WTO law, see, Chapter 5 of the present thesis.

¹⁷³*Ibid.*, *supra* note 162, para. 3.34.

confusion in existing tariff classification system and also in the context of tariff negotiations in accordance with tariff position set by the GATT system.¹⁷⁴ Japan argued that if an introduction of tariff sub-classification based on "end-use" criteria was allowed to be treated as like products under GATT, one could make a similar assertion with regard to any tariff item and many nations' tariff schedules would be found to be in violation of Article I.¹⁷⁵

Japan therefore feared that any moves to introduce tariff sub-classifications based on "end-use" criteria, would have the result that negotiators, when considering a concession-request on a given tariff position, would have to examine for "likeness" with the product covered by the requested position, with all other products covered under any other tariff position, and if there existed such "like" products, the negotiators would then have to decide whether or not they would be in a position to grant the concession, bearing reciprocal obligations in mind.¹⁷⁶ If such a situation were to happen, negotiations on tariff concessions might be overly complicated, and its operation would certainly be difficult.

The Panel, in principle, supported Japan's contention which was based on the existing practice of tariff negotiation under GATT. The Panel indicated its stance by stating that it is "*...impossible to appreciate fully the Canadian complaint if it had not in a preliminary way clarified the bearing of some principles of the GATT system in relation to tariff structure and tariff classification*".¹⁷⁷ Nonetheless, this case invited a number of objections and discussions over the findings of the Panel. The present case left room for further analysis concerning the issue of the relationship between the obligation of Article I:1 and tariff structure and classification.

The meaning of the present case could be summarised:

¹⁷⁴*Ibid.*, para. 3.31.

¹⁷⁵*Ibid.*, para. 3.21; and see a hypothetical case raised by Japan in para. 3.35.

¹⁷⁶*Ibid.*, para. 3.32.

¹⁷⁷*Ibid.*, para. 5.7.

Victory for Japan was an anomaly, Japan being involved as a respondent. Notably, Japan followed a rule-oriented approach throughout the panel proceedings. One may assume Japan must have gained some confidence in utilising GATT rules especially after this case (which came after its experience of a series of defeats in major cases during that decade). Accordingly, this case could be regarded as one of the earliest key cases which offered Japan another prospect of success in settling trade disputes. In other words, the present case was a prelude to Japan's new policy on trade dispute settlement (i.e. rule-oriented) which proved successful as will be demonstrated in the following cases in this and the next chapters.

7.1.1.6. The Beef and Citrus Case - Restrictions on Imports of Beef and Citrus Products (United States v. Japan)¹⁷⁸

Despite the fact that the Beef and Citrus case was settled bilaterally, it should be considered as a significant and essential case in demonstrating a transformation of the Japanese approach towards dispute settlement under the GATT/WTO systems. To understand the process by which the case was settled bilaterally, one must look at it from various angles. To start with, a brief summary of the dispute needs to be given. The United States claim against Japan was that quantitative restrictions on beef and citrus products did not fulfil the requirements of exceptions for price-support programmes under GATT Article XI:2(c), thereby being in violation of Article XI:1. Moreover, the U.S. also claimed that mixing requirement, according to the MAFF's practice, for orange juice (i.e. requiring bottlers to mix imported concentrate with domestic *mikan* juice) violated GATT Article III:5. The quantitative restrictions on these products had been the subject of previous bilateral complaints brought by the U.S., which were settled bilaterally by short-term agreements expanding quotas. The last agreement had expired on 31 March 1988. Thus, the U.S. took action concerning this quota issue. A Section 301 petition was filed by the Florida citrus industry after a GATT case had been filed and a panel was established on 4 May 1988.¹⁷⁹ Nonetheless, the parties reached a settlement, and thus

¹⁷⁸Complaint was made on 29 March 1988 (L/6322).

the complaint was withdrawn on 7 July 1988.¹⁸⁰ As a result, Japan agreed to remove its quantitative restrictions on those products within a few years. With respect to beef imports, those would be subject to possible tariff increase in the event of the volume of imports increasing over a designated level. Furthermore, Japan also agreed to reduce some tariffs on citrus products, and abolish the mixing requirement for orange juice.¹⁸¹

As explained above, the bilateral settlement was reached in a conventional manner (the way the two countries often relied on for settling their disputes), by political factors as well as "threats" under the U.S. Section 301. Nonetheless, to reveal the importance of this case, we shall examine it from a wider perspective, taking into account, political negotiations, both domestic and international, which lay behind this final settlement,¹⁸² linkage with other GATT cases and the political environment in Japan at that time.

Let us first look at a few cases which have a strong link with the present case. Among others, the Agriculture case ('86) and the Semiconductor Retaliation case ('87), are worth noting. The Beef and Citrus case was initiated in March 1988¹⁸³ by the U.S. request for a panel and was established in May 1988.¹⁸⁴ While, before filing that case, there was the Agriculture case in which the panel found that for 10 of the 12 product group, the GATT rules did not permit the import restrictions that were in place; in addition, the panel found that the quota on prepared and processed beef was illegal under the GATT because the Japanese government, in fact, was promoting

¹⁷⁹C/M/220 (4 May 1988).

¹⁸⁰L/6322/Add.1.

¹⁸¹L/6370 (8 July 1988): USTR, Report 301-66.

¹⁸²Amelia Porges noted in her article that "...bilateral pressure and domestic politics are both essential to explaining the result of trade negotiations. [The Beef and Citrus case] also offers examples of creative interaction between the domestic and international levels, as well as 'aggressive multilateralism' (utilisation of the GATT) to achieve very specific goals in a bilateral negotiation." in Porges, Amelia., "Japan: Beef and Citrus" in Bayard, Thomas O. and Kimberly Ann Elliot (eds.) with contributions by Amelia Porges and Charles Iceland, Reciprocity and Retaliation in U.S. Trade Policy [hereinafter, the "Reciprocity and Retaliation"], Institute for International Economics, Washington, DC, Sept. 1994, pp. 233-266.

¹⁸³L/6322, *supra* note 178.

¹⁸⁴C/M/220, *supra* note 179.

beef production instead of reducing it. The panel report was adopted on 2 February 1988.¹⁸⁵ This negative result put Japan under a great deal of pressure when the U.S. filed the Beef and Citrus case to the GATT because, for Japan, those two products, dairy products and starch (also "rice"), were politically sensitive, and accordingly Japan could not afford to lose the case.

Before the Beef and Citrus case, on 21 April 1987, Japan (MITI) filed the Semiconductor Retaliation dispute against the U.S. In this dispute, according to an ex-MITI official, the MITI wanted to go ahead with a multilateral settlement at the GATT.¹⁸⁶ The MITI's action showed a change in its way of dealing with trade disputes, at least, as regards the MITI which was in charge of the dispute. However, as explained earlier, due to the greater importance of agricultural quotas on dairy products and starch, there was some serious bargaining between the Ministries, particularly between the MAFF and MITI, as to how the government should approach the ongoing cases, the Beef and Citrus (MAFF/MOFA) case and the Semiconductor Retaliation dispute (MITI).

The Prime Minister's Office (or "*Kantei*" in Japanese) supported a bilateral settlement involving quota elimination in dealing with the Beef and Citrus issue, while, the LDP (Liberal Democratic Party which was the ruling party at that time) preferred the issue to be settled in the GATT (multilateral settlement) due to its merit from a responsibility point of view.¹⁸⁷ Nonetheless, there was a turning point for the LDP during April 1988. Certain factors persuaded the LDP to agree to a bilateral solution (thus, avoiding the question of proceeding to the GATT and a multilateral resolution):

¹⁸⁵C/M/217; before this adoption (for the entire ruling), Japan first offered a partial adoption of the panel ruling as to 10 of 12 products, i.e. excluding dairy products and starch, though, the other cps objected.

¹⁸⁶An interview with a former MITI official, June 1998, Geneva.

¹⁸⁷See, Porges, Amelia., "Japan: Beef and Citrus" in the *Reciprocity and Retaliation*, *supra* note 181, at 250, "A bilateral settlement would be the responsibility of the [LDP], nonetheless, if the GATT were to decide that the quotas were illegal, the Dietmen could plead *force majeure* and let the [MAFF and MOFA] take responsibility for a losing the case."

- i) "MAFF and MOFA bureaucrats campaigned to persuade LDP Dietmen that bilateral negotiations were better than a multilateral solution, i.e. going to GATT;
- ii) "Prominent members of the '*nourin-zoku*' [the agriculture 'clan' ("*zoku*") of LDP Dietmen] argued the need to face up to quota elimination and make a positive policy for adjustment;
- iii) "On 10 April, the LDP won a by-election by a wide margin in a citrus district in Saga;
- iv) "The LDP were reassured by the farm vote after the victory in the election, and could talk freely about quota elimination;
- v) "Most importantly, an evolution of a post-quota elimination deal worked out among the ministers and the LDP (i.e., oranges would be liberalised in five years, and beef in three years)."¹⁸⁸

After the bureaucrats' campaign with support from the Prime Minister's Office, the LDP became in favour of bilateral settlement in the Beef and Citrus issue. As a result, the bilateral solution of the present issue became a priority for the Government. Accordingly, the Semiconductor Retaliation dispute that had been filed earlier by the Japanese government (MITI) to the GATT became a key issue in order for Japan to succeed in a bilateral settlement with the U.S. on the Beef and Citrus issue. Eventually, despite the MITI's strong preference for multilateral settlement in dealing with the Semiconductor Retaliation dispute, the Japanese government reached a deal with the U.S. government on the Beef and Citrus issue bilaterally in return for the MITI's retreat from the Semiconductor Retaliation case.¹⁸⁹ In other words, the MITI had to give up its multilateral approach towards settlement in that dispute. Finally, the U.S. government withdrew its complaint on the Beef and Citrus issue due to its settlement with Japan over the Japanese claim in the Semiconductor Retaliation. In short, the Japanese government (MITI) could not make its initial step (or missed a good opportunity) towards a multilateral approach for dispute settlement under GATT.

¹⁸⁸See, *ibid.*, pp. 250-251.

¹⁸⁹Interviewed with a MITI official, Geneva, June 1998.

7.1.2. Japan as a "Claimant"

Among other cases/disputes under the category in which Japan was involved as a "claimant",¹⁹⁰ the Parts and Components case ('88) became a landmark case since it was a clearly successful performance and achievement on Japan's part in its dispute settlement history during the GATT period. Apart from that case, one may also examine the Semiconductor Retaliation dispute which illustrated the earliest sign of Japan's new approach towards trade dispute settlement. This section mainly examines one dispute and one case in order to demonstrate Japan's transformation in its policy on a dispute settlement, i.e. from "bilateralism" to "multilateralism". The rest of the cases¹⁹¹ in this category will be listed in the Appendix IV at the end of the thesis.

7.1.2.1. The Semiconductor Retaliation Dispute - Unilateral Measures on Imports of Certain Japanese Products (Japan v. United States)¹⁹²

The Semiconductor Retaliation dispute, as has been mentioned in Section 7.1.1.6., is closely related to the bilateral settlement in the Beef and Citrus case.

Japan claim against the U. S. was that an American tariff increase on certain Japanese products was discriminating and in violation of GATT Articles I and II. Increases in the U. S. tariff were introduced in retaliation for alleged violations of the Japan-U.S. Semiconductor Arrangement signed on 2 September 1986 and finalised in exchange for the suspension of three dumping proceedings against Japanese semiconductor imports to the U. S. and a Section 301 proceeding launched by the U. S.

¹⁹⁰According to WTO Secretariat statistics, Japan brought 8 consultation requests (7 distinctive matters) under the GATT 1947 including the Tokyo Round Code (Nevertheless, a complaint made under the Code will not be examined in the main text of this thesis).

¹⁹¹For example, the Zenith case, in which Japan had a positive outcome, showed the possibility that a national court could play a role in resolving disputes. In this case, the GATT/WTO law was referred to as a criterion in a domestic court; another case, i.e. EEC-Import restrictive measures on video tape recorders (the "Poitiers" case) was settled bilaterally, see the list of cases in Appendix IV to the thesis.

¹⁹²Complaints were made on 21 April 1987 (L/6159); for relevant articles, see Kingery, John C., "The U.S. - Japan Semiconductor Agreement and the GATT: Operating in a Legal Vacuum", 25 Stan. J. Int'l L. (1989), pp. 467-497; Dallmeyer, Dorinda G., "The United States - Japan Semiconductor Accord of 1986: The Shortcomings of High-Tech Protectionism", 13 Md. J. Int'l L. (1989), pp. 177-222; also for a case related, see EC v. Japan: Restrictions on Semiconductors in Section 7.1.1.4. of the thesis.

Semiconductor Industry Association (SIA) against Japanese barriers to American imports.

In this dispute, the U. S. claimed that, under the Arrangement, Japan had violated obligations which were: (i) to open its semiconductor market (improving access to the Japanese market); and (ii) to stop dumping semiconductors in third markets (monitoring exports).¹⁹³ The U. S., therefore, increased its tariff to 100% *ad valorem* on a \$300 million portion of the market in trade which represented the value of the trade loss claimed for a breach of Japan's obligations. Japan, however, took a "wait and see" stance, in that it did not request a panel, which presumably was because of the ongoing issues with the U.S., i.e. the result of the Agriculture case and the priority given to success in a bilateral settlement of the Beef and Citrus issue. Meanwhile, the U. S. had abolished a tariff increase on trade valued at \$51 million in June 1987 and a further \$84 million in November 1987 in recognition of the Japanese agreement in compliance with the antidumping obligation of the bilateral agreement. Removal of the remaining tariff increases on trade valued at \$165 million became effective on 1 August 1991 in response to the conclusion of an extension of the bilateral agreement that contained a further commitment to accomplish the objectives of market access.¹⁹⁴ Some of the U. S. actions in response to the dispute were withdrawn when Japan eventually acceded to the U.S. demands, while other actions remained for five years until the U.S. gave them up.

With regard to the manner of settlement, it is important to note that the Prime Minister's Office and MAFF/MOFA dissuaded the MITI from bringing the dispute to GATT (where a multilateral solution could be withdrawn) because there was a fear that the U.S. might bring another crucial issue regarding "rice" to GATT.¹⁹⁵ After the defeat in the Agriculture case, Japan wanted to avoid particular issues, such as, the "rice" issue since that issue was closely linked to the domestic vote from farmers. As

¹⁹³Both obligations under the bilateral agreement became a central issue in the Semiconductor case between the EC and Japan, which are dealt with in Section 7.1.1.4 of this thesis.

¹⁹⁴BNA, 8 ITR 888 (1991).

¹⁹⁵An interview with a former MITI official (May 1997, Geneva)

explained earlier in Section 7.1.1.6. (the Beef and Citrus case), as a priority, Japan needed, above all, to reach a bilateral settlement on that issue. Thus, the settlement of the present case was more political (or bilateral) than legalistical (or multilateral). In other words, the political deal among Japanese Ministries seemed to have interrupted MITI's further multilateral action at GATT. If Japan had decided to further a multilateral approach to resolving disputes, the result might have been different. Moreover, if Japan had maintained its multilateral approach in the present case to the end, it could have marked a starting point in Japan's new approach to dispute settlement under GATT, which could be seen as a transformation from "bilateralism" to "multilateralism", from "power-oriented" to "rule-oriented" and from "non-legalistic" (i.e. "political" or "power-oriented") to "legalistic".

7.1.2.2. The Parts and Components Case - Antidumping Regulation on Imports of Parts and Components (Japan v. European Community)¹⁹⁶

This case became one of the most important cases in Japanese dispute settlement history under GATT/WTO since the claim was initiated by Japan under GATT Article XXIII:2 for the first time, and concluded with Japan's first clear victory at GATT. The present case confirmed a turning point in Japan's dispute settlement history. Since that victory, Japan's attitude towards trade dispute settlement has indeed changed. Japan certainly increased its confidence in utilising the multilateral approach towards settling disputes. One could describe this transformation in Japan's approach as a shift from "bilateralism" to "multilateralism"; "power-oriented" to "rule-oriented"; and "non-legalistic" to "legalistic".

¹⁹⁶Complaints was made on 8 August 1988 (L/6381); Article XXIII of the GATT and Antidumping Code complaints were merged in this case; L/6657 (22 March 1990) in **BISD 37S/132-99 (1991)**; for an article related, see Petersmann, Ernst-Ulrich, "Settlement of International and National Trade Disputes Through the GATT: The Case of Antidumping Law" in E.-U. Petersmann and G. Jaenicke, (eds.), Adjudication of International Trade Disputes in International and National Economic Law, University Press Fribourg, Switzerland, 1992, pp. 77-138; Iwasawa, Yuji., WTO no Funso Shori, Sanseido, (in Japanese), Tokyo, 1995, Chapter 6, pp. 187-197.

Summary of Facts and Procedure:

During the early 1980's, as a response to the traditionally high tariff and non-tariff barriers imposed on certain products in Europe, Japan began to invest seriously in production and assembly facilities in the EC.¹⁹⁷ The EC, however, complained that antidumping orders on finished products were being circumvented by importing parts and assembling them locally in the EC.

To respond to this situation, the Council of the European Community (hereinafter, the "Council") adopted a regulation (hereinafter, the "Screwdriver Regulation")¹⁹⁸ to amend the antidumping laws of the EC.¹⁹⁹ The Screwdriver Regulation allows for the application of antidumping duties on products assembled in the EC subject to certain criteria²⁰⁰ provided for in Article 1. The aim of the new law was to regulate the practice by which certain exporters of products to the EC were alleged to avoid antidumping duties by producing the products inside the EC out of mainly imported components under a technique called "Screwdriver Assembly Technique". The extension of antidumping laws with respect to products assembled in the EC was regarded as a new strategy for the EC whose market was struggling with the growth

¹⁹⁷For the history of the Screwdriver Regulation (*infra* note 199), see McDermott, Patrick J., "Extending the Reach of Their Antidumping Laws: The European Community's 'Screwdriver Assembly' Regulation", 20 Law & Pol'y Int'l Bus (1988), pp. 316-319.

¹⁹⁸Protection Against Dumped or Subsidised Imports, Council Regulation No. 1761/87, 30 OJ L167, 1987, p. 9.

¹⁹⁹The Screwdriver Regulation (Council Regulation No. 1761/87) amended the basic European Community antidumping and countervailing duty law, i.e., the addition of a new paragraph 10 to Article 13 of Council Regulation No. 2176/84, 27 OJ L201, 1984, p.1 [hereinafter "Council Regulation"] and its successor Council Regulation (EEC) No. 2423/88, OJ L209, 1988 (i.e. the provisions of Council Regulation No. 1761/87 were incorporated into Regulation No. 2423/88 in Article 13:10).

²⁰⁰Article 13:10(a) of the Council Regulation No.2423/88 provides that certain measures may be taken if the following conditions are met:

Definitive antidumping duties may be imposed [...] on products that are introduced into the commerce of the Community after having been assembled or produced in the Community provided that:

- assembly or production is carried out by a party which is related or associated to any of the manufacturers whose exports of the like products are subject to a definitive antidumping duty;
- the assembly or production operation was started or substantially increased after the opening of the antidumping investigation; and,
- the value of parts or materials used in the assembly or production operation and originating in the country of exportation of the product subject to the antidumping duty exceeds the value of all other part or materials used by at least 50%.

of Japanese products.²⁰¹

Japan brought a complaint against the European Community to the GATT claiming that the imposition of antidumping duties on certain products assembled inside the EC, on the basis of the antidumping order was not authorised by GATT Article VI or Article XX(d) and therefore, resulted in violation of GATT Article I, II, III, and VI. Japan also claimed that the local content requirement of over 50% to avoid antidumping duties on products assembled inside the EC was considered as an internal requirement which imposed unfair treatment on imports in violation of Article III:4. While, Japan also challenged the imposition of antidumping duties on locally assembled products because the GATT Antidumping Code does not cover products manufactured inside of a customs area such as the European Community, in other words, the Code only deals with imports. Nonetheless, this claim under the Antidumping Code did not proceed due to a lack of findings of dumping and injury required by Article 1 of the Code.

In the present case, Japan made a claim under two different rules: (i) GATT Article XXIII, (ii) Article 15 of the Antidumping Code (Consultation, Conciliation and Dispute Settlement). On 10 October 1988, despite a Japanese request for conciliation regarding the Antidumping Code under Article 15(3), the EC refused to agree. The reason for the EC's refusal was that the enforcement measures authorised by GATT Article XX(d) were not subject to the Antidumping Code. Furthermore, under GATT Article XXIII, a panel was already being established to deal with the same issues.²⁰² As a consequence of the EC's refusal, Japan did not maintain its assertion

²⁰¹First four antidumping investigations can demonstrate the situation: see investigations on 'Electronic Scales', 30 OJ, C235, 1987, p. 3; 'Electric Typewriters', 30 OJ, C235, 1987, p. 2; 'Hydraulic Excavators', 30 OJ, C285, 1987, p. 4; 'Photocopiers', 31 OJ, C44, 1988, p. 3.

²⁰²What would have happened if two panel were established on the same issue? In this case, even after setting up a panel under GATT Article XXIII:2, Japan still requested Antidumping Code conciliation under Article 15(3) of Antidumping Code. With respect to the matter in question, Jackson described such situation as "Balkanisation" in the GATT dispute settlement procedure. He explained in his article that the GATT dispute settlement system became complexed and segmented as a result of each dispute settlement procedure defined under Tokyo Round Code. This problem brought up the issue of "rule-shopping" for a dispute settlement. For further argument on this point, see Jackson, J. H., "The Birth of the GATT-MTN System: a Constitutional Appraisal", 12 L. Pol'y in Int'l Bus., 1980 at 21, 44.

any further regarding the Antidumping Code.²⁰³

Summary of Findings and Conclusions:

-The anti-circumvention duties (hereinafter, the "duties")²⁰⁴ levied on products assembled within the EC were not 'border tariffs' stipulated in GATT Article II but 'internal taxes' under Article III:2. These duties were imposed on imported goods alone, thus they were in violation of national treatment concerning 'internal taxes' under Article III:2 unless otherwise stated.

-With regard to the local content requirement needed to avoid new Antidumping measures, these were considered to be internal requirements under GATT Article III:4 because such requirements were required only to imported goods. Accordingly, the requirements were in violation of 'no-less-favourable' treatment of Article III:4.

-The validity of GATT Article XX(d) stated that it could only authorise the use of measures necessary to secure compliance with laws or regulations consistent with the General Agreement, which can be regarded as the core of this panel decision.²⁰⁵ Thus, although this Article could justify the use of measures (as general exceptions), in order to enforce the proper imposition of Antidumping duties, it did not authorise imposition of those duties beyond the scope of existing Antidumping orders for the broader purpose²⁰⁶ of accomplishing the underlying objective of Antidumping laws.

²⁰³Imagine that two different panels were established concerning the same issue based on two different rules and issued different decisions, it would have been controversial (see, *ibid.*, the "Balkanisation"); there was such a case, though, it was slightly different from the above hypothetical case, namely, each panel (i.e. one was under the General Agreement and the other was under the Licensing Code) examined a different issue, see the parallel complaints made by the U.S. against (i) India - Import Restrictions on Almonds (under GATT XXIII) and also against (ii) India - Import Licenses on Almonds (under the Licensing Code). See for complaints (i) which was made on 17 June (C/M/211) and was withdrawn due to the bilateral settlement on 8 June 1988 (C/154/Add.1), see for complaints (ii) which was made on 17 June 1987 (C/M/211) and was withdrawn on 9 June 1988 (LIC/15).

²⁰⁴For "Anticircumvention Measures", see Jackson, et al., *Int'l Econ. Relations*, *supra* note 138, pp. 712-714.

²⁰⁵*Ibid.*, paras. 5.14-5.18.

²⁰⁶Note, the panel's narrow interpretation of GATT Article XX(d) which defined exemption, in contrast, the panel made an interpretation broadly for GATT Article III:4 which defined requirements.

(i.e. the Panel's conclusion meant that the qualification under Article XX(d) should not be interpreted so as to mean ensuring attainment of the objectives of laws and regulations, but, rather, to enforce obligations under laws or regulations consistent with the General Agreement). Thereby, the EC measures taken to avoid circumvention were not authorised under Article XX(d).²⁰⁷

-The EC had declined to justify the measures in question under GATT Article VI, therefore the panel did not consider this issue.²⁰⁸

-Decisions on other claims (e.g. the issue concerning lacking of transparency in Article 13:10 of the Council Regulation under GATT Article X (1) and (3); the issue of illegality of the existence of Article 13:10 of the Council Regulation) brought by Japan²⁰⁹ were unnecessary due to the above ruling.

Remarks on the case:

The EC agreed to adopt the panel report. Nevertheless, the EC stated that it would defer compliance with the report until the completion of undergoing negotiations concerning the Antidumping Code at the UR.²¹⁰ The issue of "circumvention" was then under negotiation at the UR. Pending the outcome, the EC maintained its existing circumvention regulations. In other words, the EC did not comply with a decision made by the GATT panel. Although Japan's defence was successful in this case, the EC, decided to take advantage of the leeway existing in the rules taken in force, at least, until the introduction of any new rule.

²⁰⁷The application of GATT Article XX(d) was already denied in the case: United States v. Canada: Administration of the Foreign Investment Review Act [FIRA] in BISD 30S/140 (1984).

²⁰⁸"In conformity with the practice of panels not to examine exceptions under the General Agreement ... and not to examine issues brought only by third parties (the U.S. in the present case)" in *ibid.*, para. 5.11; see also, *infra* note 215.

²⁰⁹Japan must have been concerned with this particular issue because if the panel took up the issue in the present case, it could have indicated a certain direction on the legality of the U.S. Section 301 under GATT. In addition, the unilateral measures was one of the contentious issues at then ongoing Uruguay Round negotiations; cf. DSU23.

²¹⁰See for more examples, United States v. European Community: Production Aids on Canned Peaches, Canned Pears, Canned Fruit Cocktail and Dried Grapes, 19 March 1988, (L/5306); see also the Agriculture case (Section 7.1.1.3. of this thesis) in which Japan showed a similar behaviour as the EC took in the present case for implementation of the panel's decision due to then ongoing UR negotiations.

CHAPTER 7

Taken as a whole, Japan opened a new era in its dispute settlement history after having experienced a series of defeats (with the exception the anomalous success in the SPF case in which Japan was a "respondent" in July 1989). In this regard, this decade eventually became a symbolic turning point in Japan's dispute settlement history.

It is interesting to note that this new Japanese attitude towards dispute settlement (i.e. more "rule-oriented", "multilateral" or "legalistic" approach) coincided with an institutional as well as constitutional transformation from GATT to WTO by virtue of the UR negotiations. This can be also described as the institutional/constitutional transformation, i.e. "judicialisation" (from "pragmatic" to "legalistic"), as regards the resolution of trade disputes. Presumably, there might have been a certain link between the change in Japan's attitude towards trade disputes settlement and the institutional/constitutional transformation (i.e. from GATT to WTO). If so, with a strong trend towards increasing demand for multilateralism in world trade compelled with the lessons learnt through bitter experience at the GATT panels during the 80's, Japan must have realised not only the importance of multilateralism but also its effectiveness in the fiercely competitive environment of the world trade scene, and its role in protecting Japan's national interests utilising GATT/WTO rules.²¹¹

In fact, in this case, although Japan had achieved a successful result under the GATT system, Japan was also presented with one of the defects of the GATT dispute settlement mechanism (mentioned in Chapter 2), that is, a lack of enforcement power, whose presence might have brought about a different outcome under the new WTO system.²¹² Furthermore, it would have been more difficult for the losing party (the EC in this case) to defer its compliance with the panel's decision unless, for example, it could have afforded compensation which is provided for in a provision of

²¹¹See, in general, Japan's commitment to the multilateral trading system and to the active participation in then on-going UR negotiations on dispute settlement, in TPRM on Japan (C/RM/M/8 8 October 1990) at paras. 7 and 151.

²¹²Apparently, the issue of enforcement, in particular, an "implementation" issue is currently under discussion at the WTO by virtue of the Banana case. This case indeed revealed the margin of DSU procedure; for further detail about the case can be found in Conclusion of the thesis and under its footnote 4. As of 29 January 1999, the U.S. and EU did not give in to each other, thus no settlement has yet been reached.

the DSU.²¹³

Furthermore, a few more points concerning the present case should be pointed out. First, Japan's trust in the effectiveness of GATT dispute settlement procedures must have increased since it was the first case that Japan had brought under Article XXIII:2 of GATT, and furthermore the first case in which Japan had been favoured. Second, in the present case, unlike its usual approach, Japan demonstrated a rule-oriented, legalistic or multilateral approach under GATT. Despite the small number of precedents in GATT panel dealing with anti-dumping matters, Japan took the brave step of initiating an action and bringing a case before the panel to resolve anti-dumping measures which had long been a contentious issue under GATT. In other words, Japan sought a settlement of this dispute within a multilateral framework, i.e. GATT. This is a significant step in terms of Japan's dispute settlement history under the GATT system since most of the Japanese cases were resolved bilaterally before reaching a judicial stage (i.e. a panel). The fact that Japan did bring the alleged EC antidumping regulation to a GATT panel can be regarded as a clear indication of a belief in multilateralism, in other words, a departure from Japan's traditional "bilateral" approach.²¹⁴ Third, the Panel did not examine the consistency of the EC measures with Article VI (on the basis of the practice of panel, i.e. "not to examine exceptions under the General Agreement which have not been invoked by the contracting party complained against"²¹⁵ and "not to examine issues brought only by third parties"²¹⁶), nonetheless, it made clear that those measures were inconsistent with Article III and were not justified under Article XX(d). The present

²¹³See, Article 22 of the DSU; Note that Japan did offer some form of compensation to the U.S. for the longer implementation period in Japan Alcohol-II case regarding Mutually Accepted Solution on Modalities for Implementation, see (Japan's communication to the U.S.) in WT/DS8/19; WT/DS10/19; WT/DS11/17 (12 January 1998), and see also (Japan's communication to Canada) in WT/DS8/20; WT/DS10/20; WT/DS11/18 (12 January 1998).

²¹⁴According to a MITI official, there was less resistance for Japanese government to bring the issue to GATT because its claim was not against the U.S. (which normally contains more sensitive political nature) but against the EC, which might, to some extent, psychologically influenced on Japan's behaviour in the present case. (This interview was conducted in June 1998, Geneva).

²¹⁵See, United States - Import Sugar from Nicaragua in BISD 31S/74, para 4.4.

²¹⁶Cf. United States - Restrictions on Imports of Sugar in BISD 36S/331 (L/6514), para. 5.9.

case, therefore, could be considered as a landmark case which gave a clear warning to protectionists not to abuse anti-dumping measures under Article VI.

Nevertheless, the question remains as to why the EC did not choose to justify its measures under Article VI rather than justifying them under the provision of general exceptions provided for in Article XX(d) which requires a contracting party to meet with strict requirements. One speculation which could be made is that the EC might have preferred the panel to be silent on the question of the legality of anti-circumvention measures because of then ongoing Antidumping Code negotiations at the UR. In short, the EC simply wanted to avoid the Panel's pre-emptive influence over that issue at the UR. Furthermore, by not referring to Article VI to justify the anti-circumvention measures at the panel proceedings (and even at the cost of losing the case as it actually happened), the EC might have thought that it could have kept open the possibility of the legality of the measures at issue for the time being, at least, until the conclusion of the UR negotiations.²¹⁷

To sum up, after this first clear legal victory obtained in the present case, Japan confirmed its new policy regarding trade dispute settlement (i.e. a "multilateral" approach) under GATT/WTO dispute settlement system. Furthermore, Japan had gained substantial confidence from this particular victory, as one can see from the cases under WTO, which will be examined in the next chapter.

²¹⁷The provisions on anti-circumvention were on the agenda for the UR negotiations on the Anti-Dumping agreement, as well as the Agreement on Subsidies and Countervailing Duties but no agreement was reached. The GATT 1994, therefore, does not have a provision on anti-circumvention, nonetheless, the Final Act deals with this issue; it recognised that "the desirability of the applicability of uniform rules in this areas as soon as possible", and further decided to refer this matter to the Committee on Anti-Dumping Practices established under that Agreement for resolution. See, **Ministerial Decisions and Declarations, Decisions and Declaration Relating to the Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994 (Decisions on Anti-Circumvention)**.

Chapter 8. CASE STUDIES: JAPANESE TRADE DISPUTES

UNDER WTO - A NEW JAPAN'S POLICY ON DISPUTE

SETTLEMENTS

8.1. Japan's Experience of WTO Disputes¹

This chapter undertakes WTO case studies whose main goal is to demonstrate how the new DS mechanism actually worked. This study also reveals Japan's new policy on DS under the WTO. An early sign of this transformation which emerged in Japanese policy during the GATT period has already been identified in the previous chapter (for example, in the Semiconductor Retaliation dispute in 1987). Japan's new policy on DS characterised as "multilateralism" became even more obvious through a victory for Japan in the Parts and Components case ('88), and, further, this policy has been followed in every Japanese case dealt with under the WTO system. To illustrate the Japanese "multilateral" approach in settling disputes, what I consider are the most significant disputes have been selected and are examined in this chapter, those cases being: the Auto dispute, the Alcohol Beverage (or "Alcohol-II") case and the Film case.²

8.1.1. Japan as a "Claimant"³

8.1.1.1. The Auto Dispute

The present dispute between Japan and the U.S. over car and car parts was the first case in which Japan (the Claimant) was involved under the WTO system.⁴ Although

¹According to WTO Secretariat statistics (as of 10 June 1998), Japan was involved in 23 cases including those cases in which Japan has been involved as a "third party" (18 distinctive cases). As of 5 June 1998, the WTO Secretariat recorded, in total, 135 consultation requests. Accordingly, on the basis of the statistics above, the rate of Japanese involvement in a WTO case is 17%.

²The cut-off date for the WTO case studies based upon in this thesis is 30 June 1998; see Appendix III of the thesis for the new cases in which Japan has been involved after this cut-off date, i.e., the "Indonesian National Car" case and the "Japan Apple" case.

³According to WTO Secretariat statistics (as of 10 June 1998), Japan became a "complainant" in 5 cases (4 distinctive cases) out of 23 cases (22%).

⁴Articles on this dispute can be found in, *The Economist*, May 13th-19th 1995 at 18, 79-80; *ibid.*, May 20th-26th 1995 at 81; *ibid.*, June 17th-23th 1995 at 97; *ibid.*, June 24th-30th 1995

the dispute was eventually settled through bilateral negotiations outwith the WTO process, this dispute contains a number of important aspects which illustrate Japan's new policy on DS. For instance, it was the first dispute in which a Section 301 (unilateral measures) was challenged under the WTO DS mechanism, and moreover, by Japan.

To grasp the whole picture of this dispute, an overview of the present dispute⁵ is given (*emphases added*):

- **5 May, 1995**: U.S. trade representative Mickey Kantor called off the talks with Japan to be held in Whistler, Canada, after the two parties failed to agree on granting the U.S. wider access to Japan's network of car dealers and on deregulation of Japan's replacement car parts market.

- **7 May**: Ryutaro Hashimoto, the Japanese minister for MITI, said that *Japan would take the dispute to the WTO if sanctions were imposed by the U.S.*

- **10 May**: The USTR issued its determination (certain acts, policies and practices of Japan restrict or deny U.S. auto parts suppliers access to the auto parts replacement and accessories market in Japan, and are unreasonable and discriminatory) under Section 301 and 304 of the U.S. Trade Act. In the meantime, M. Kantor sent Ruggiero (the current DG of WTO) a notification informing him of the U.S. intention to bring the issue against Japan to the WTO.

- **16 May**: The U.S. announced under the affirmative determination that it would impose a 100% tariff on 13 Japanese luxury cars models unless Japan opened its market to U.S. cars and car parts (setting 28 June as the deadline for a final determination of the imposition of a 100% punitive tariff).

- **17 May**: *Japan requested the U.S. to enter into urgent consultations under GATT Article XXII:1 and Article 4 DSU⁶ in Geneva by 29 May to discuss the legality of U.S. sanctions and added that it reserved its right to retaliate.*

- **26 May**: The U.S. rejected Japan's request but offered talks on 20 June in Washington.

at 95; also in WTO, WTO Focus, (No. 3) May-June 1995.

⁵See, this outline of the events is mainly based on, "Japan's carmakers to buy more parts abroad", the Financial Times, 29 June 1995 at 5.

⁶Request for Consultations by Japan, WT/DS6/1 (22 May 1995).

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- **27 May:** Japan refused the U.S. proposal and replied that talks should be held in Geneva within the framework of WTO.
- **12 June:** The parties showed no sign of compromise during the talks as agreed on 2 June. *Japan said it would not negotiate under U.S. threat of actions* (The first round of Article XXII consultations in Geneva with the participation of Australia as a third-country,⁷ nonetheless, the U.S. rejected the EC request to participate⁸).
- **15 June:** No agreement was reached at the G-7⁹ summit held in Canada. President Clinton said sanctions would come into effect on 28 June if talks failed. Prime Minister Murayama said that *sanctions were invalid according to international rules*.
- **22-23 June:** The second round of Article XXII consultations was held in Geneva (with Australia as a third-country participant).
- **28 June:** Agreement (The Japan-U.S. Framework Talks on Auto and Auto Parts) was reached "in essence"¹⁰ just hours before deadline for the sanctions to come into effect. The U.S. "threats", i.e. an imposition of 100 % tariff on Japanese luxury cars unless Japan provided the U.S. with access to its car and car parts market, was dropped.

As emphasised in italics above, to the U.S.'s surprise, Japan took an "assertive" attitude throughout the latest car talks with the U.S. within a multilateral framework despite the "threat" of Section 301. This indeed demonstrated Japan's new policy on DS supporting a "multilateral" instead of a "bilateral" approach as had been the case during most of the GATT period. This consistent as well as determined multilateral attitude stands in contrast to its policy taken in the Semiconductor issue ('85) which Japan regrettably gave in to U.S. "threats" under Section 301, and ended up signing

⁷Request for consultations under Article 4:11 DSU - Communication by Australia (1 June 1995), WT/DS6/3 (12 June 1995); Acceptance of the Request to Join Consultations - Communication by the U.S., WT/DS6/4 (14 June 1995).

⁸Request to Join Consultations under Article 4:11 DSU - Communication by the EC (31 May 1995), WT/DS6/2 (2 June 1995).

⁹The G-7 (Group of Seven) consists of the U.S., Japan, France, Germany, Canada, Italy and the U.K. The main aim of G-7 is to set broad directions for international economic and monetary activities. While, the G-7 members hold an annual economic summit which mainly deals with economic and financial matters (including trade policies) of common interest to participants.

¹⁰For Japan- U. S. car trade accord where differences emerged over interpretation between Tokyo and Washington, "One man's promise is another's estimate", the Financial Times, 30 June 1995 at 5; "OK, Mickey, let's say you won", the Economist, July 1st-7th 1995 pp. 81-2.

the Japan-U.S. Arrangement on Semiconductors (July '86) which was renewed once in August '91 and eventually continued until the end of July '96.¹¹ In April '87, however, Japan retaliated against the U.S. discriminatory tariff increases on bound items.¹² Nevertheless, due to its domestic political decision (i.e. priority was placed on the other ongoing dispute, namely, the Beef and Citrus case),¹³ Japan (MITI) had to abandon its claim under GATT XXIII:1 against the U.S. sanctions (which were imposed because of failure to comply with the Arrangement). If Japan had exhausted the GATT panel procedures, that case would have yet an epochal precedent illustrating Japan's new policy on DS without having to wait for another year when Japan achieved its first legal victory in the Parts and Components case.¹⁴ In any event, Japan undoubtedly indicated its new attitude towards DS in the present case.

Nonetheless, as explained earlier, Japan had learnt a number of lessons through previous events, especially from the mid to the late 80's, such as the Japan-U.S. Arrangement on Semiconductors ('86), the Semiconductor Retaliation dispute (Japan v. U.S.) ('87) and the Semiconductor case (EC v. Japan) ('87). Hard lessons learnt by Japan through those bitter experiences could include:

- i) VRAs ("grey-area measures" generally) were over¹⁵: The GATT panel ruled, for the first time, on the VRAs and decided they were GATT illegal;
- ii) The end of "bilateralism": This approach had been indeed effective and popular, but the EC did break its "silence" when the Arrangement between Japan and the U.S. was made (Japan make a commitment to the Arrangement containing "grey-area measures" such as VRAs and VIEs to avoid the imposition of unilateral sanctions

¹¹The day after the expiration date (31 July 1996) of the Arrangement, the U.S. and Japan agreed to have a deal on further co-operation in the Semiconductor sector, "U.S., Japan Strike Industry and Government Deals on Semiconductors", Inside US Trade, 5 August 1996.

¹²See, Section 7.1.2.1. of this thesis.

¹³See, Section 7.1.1.6. of this thesis.

¹⁴See, Section 7.1.2.2. of this thesis.

¹⁵See, *supra* note 150 (Chapter 7), the SGA (the WTO Agreement on Safeguards), Article 11 which prescribes the prohibition of grey-area measures.

process under Section 301). This was a conventional pattern for some time in the bargaining involving bilateral economic negotiations, especially as between the U.S. and Japan.¹⁶

iii) No VIE¹⁷ commitments should be made: Japan realised this point after, regrettably, signing the Arrangement with the U. S. Under this Arrangement, Japan was in a difficult position due to a so-called "side letter" which referred to a numerical target (the U.S. viewed this promise or target as "commitments" of the Japanese government), i.e. a 20 % of market share for the U.S. Semiconductor Industry, to be fulfilled by Japan .

iv) A "Multilateral" approach in line with the WTO should be followed: If Japan had sanctions imposed against it under unilateral measures (e.g. a Section 301 order by the U.S.), Japan should take such unilateral actions to a multilateral forum, namely, the WTO DS system. Japan arrived at this policy after a series of bitter experiences, in particular, the Semiconductor issue in which Japan gave in to the U.S. threat under Section 301, so that Japan could avoid going to a multilateral forum.¹⁸ Nevertheless, to Japan's utter surprise, the EC make a claim against Japan and Japan eventually lost the case at the GATT panel. In short, Japan lost two cases over the same issue on semiconductors. Meanwhile, it is worth noting that Japan accepted the opening of its "rice" market, which was a crucial issue for Japan, at the end of the Uruguay Round

¹⁶For example, the trade negotiations on textiles, colour TV sets, steel, machine tools and semiconductor.

¹⁷Voluntary Import Expansion (VIE): "A bilateral arrangement under which a country agrees, ostensibly voluntarily, to adopt measures promoting the use of imported products of particular export interest to the other country. Such arrangements appear to be taking the place of the grey-area measures which is illegal under the WTO rules (see, *ibid.*)", in Goode, Walter., Dictionary of Trade Policy Terms, 2nd ed., Centre for International Economic Studies, University of Adelaide , Australia, 1998 at 307; One could regards a VIE as a model which is developed from a VRA. VIE requires a country to reply to another's trade sanctions (i.e. a unilateral sanction such as the U.S. Section 301) by agreeing to buy more of certain items from that county. It reminds us of "mercantilism", i.e., seeking maximisation of exports, whereas minimisation of imports.

¹⁸Japan had a little doubt about the efficacy of the multilateral trading regime, see in paras. 16 and 17 in C/RM/M/8 (8 October 1990) which was reproduced in GATT, Trade Policy Review - Japan (1990), November 1990.

of negotiations. This commitment led Japan's policy on DS towards favouring "multilateralism" as well as the establishment of the WTO.

As a consequence, throughout the Auto dispute, Japan fought back against the U.S. (i.e. the threat under Section 301) with the help of its new policy on DS (i.e. "multilateralism"), which signified a significant difference from Japan's conventional attitude towards the Japan-U.S. bilateral trade negotiations. Nevertheless, the U.S. still insisted on taking the traditional approach based upon bilateralism (i.e. VRAs) in the Auto dispute. It seems that the U.S. clearly misjudged in this dispute how far Japan had transformed its attitude towards bilateral trade negotiation as well as its policy on DS.¹⁹ Japan's new approach, at last, brought it a positive outcome which was decided impartially at the multilateral table (despite the threats under Section 301). In this respect, this dispute not only marked a significant achievement but assured the beginning of a new era in Japanese DS under GATT/WTO.

8.1.2. Japan as a "Respondent"

8.1.2.1. The Alcoholic Beverage Case

For Japan, the Alcoholic Beverages case is the first case which has gone through the whole DS procedure under the new WTO DS mechanism. This case is particularly noteworthy in the sense that the same issue was ruled on by the Panel in 1986 under the GATT as examined in Section 7.1.1.2. of this thesis.²⁰ This particular case,

¹⁹As a former MITI official, Mr. Ichiro Araki (Deputy Director, International Communication Office) explicitly stated a new Japanese attitude towards the bilateral economic relations in this article, *"Yes, our present stance is inconsistent with our past action, but we are now firmly committed to rejecting managed trade and VRAs"*. He also commented that *"Ambassador Kantor just does not seem to realise how far Japan has come into fully embracing the principle of free trade on multilateral rules and disciplines"*, The New York Times, Letter to the Editor - "Japan Won't Take a Trade Back Seat Anymore", 14 May 1995; this article is also available on the Web site at [<http://www.jef.or.jp/auto/letter.html>].

²⁰Apart from the case on Japanese alcohol which was ruled under both GATT and WTO panels, there is another issue, i.e. leather, which was brought to these two different panels. One can find the first leather case in **BISD 31S/94 (1984)**, also see Section 7.1.1.1. of this thesis. While the second dispute on leather is under way, which was initiated by the EC [Japan Tariff Quotas and Subsidies Affecting Leather, **WT/DS147 (8 October 1998)**]; see OJ L159, 3.6.98, pp. 65-67 (commission decision of 19 May 1998, concerning Japanese

therefore, can provide a number of points for our studying: how the defects of the GATT mechanism has been improved on the WTO mechanism; and how Japan has changed its attitude towards DS.

8.1.2.1.1. Report of The Panel

Background

This case has been inherited from the 1987 Panel Report on Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages (hereinafter, the "1987 Panel Report" or "Japan - Alcohol-I") under the GATT 1947. The previous case was initiated by the EC's request for consultation with Japan concerning Japan's Liquor Tax Law ("Liquor Tax Law"), as it then existed. The 1987 Panel Report finally concluded that some aspects of the Liquor Tax Law were not consistent with GATT Article III:2, first and second sentences, and suggested that the CPs recommend that Japan brings its taxes imposed on whiskies, brandies, other distilled spirits (i.e. gin and vodka), liqueurs, still wines and sparkling wines into conformity with its obligations defined under the General Agreement.²¹

Accordingly, on 2 February 1989, Japan informed the CPs: the *ad valorem* tax and grading system had been abolished, resulting in a single rate for all grades of whisky/brandies; and, the existing differences in taxation between whisky/brandies and shochu had been considerably reduced by decreasing the specific tax rate for whisky/brandies and raising that on shochu. In addition, an interim measure was provided for under the Special Taxation Measures Law in order to ease the pain of adjustment for small scale manufacturers of shochu. On 1 May 1994, the Japanese government further amended the Liquor Tax Law, that is, it raised tax rates on shochu and on spirits, while tax rates on whisky remained unchanged, and also the

products in relation to trade in leather).

²¹The Panel Report on Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages (Japan - Alcohol-I), BISD 34S/83 (1988) adopted on 10 November 1987, paras. 5.5, 5.6, 5.7, 5.9, 5.11, and 5.13., which are reproduced as II.B in the Panel Report on Japan - Taxes on Alcoholic Beverages (Japan - Alcohol-II), WT/DS8/R; WT/DS10/R; and WT/DS11/R (11 July 1996).

application of the interim measures under the Special Taxation Measures Law was extended by 3 years.

Summary of Facts and Procedure:

Nonetheless, the EC was dissatisfied with the internal tax treatment even after the changes made by Japan in accordance with the recommendation of the Panel in the 1987 Panel Report. At last, on 21 June 1995, the EC requested consultations with Japan under Article XXII²² with respect to the Liquor Tax Law.²³ Subsequently, on 7 July 1995, the U.S.²⁴ and Canada²⁵ requested that they join in the consultations under Article 4.11 DSU. On 19 July 1995, Japan agreed to their request.²⁶ On 7 July 1995, Canada requested consultations with Japan pursuant to GATT Article XXIII with respect to certain Japanese liquor taxation laws.²⁷ On 17 July 1995, the U.S. and the EC requested the right to join in the consultations,²⁸ pursuant to Article 4.11 DSU. On 7 July 1995, the U.S. requested consultations with Japan under GATT Article XXIII with respect to internal taxes imposed by Japan on certain alcoholic beverages under the Liquor Tax Law.²⁹

Although the four parties held joint consultations on 20 July 1995 so as to reach a mutually satisfactory resolution concerning the matter, no solution was reached. In addition, the U.S. and Japan consulted under Article XXIII:1 on 20 July 1995, yet no mutually acceptable resolution of the matter was achieved.

The EC, on 14 September 1995, requested the DSB (Dispute Settlement Body) to establish a panel under standard terms of reference in accordance with GATT Article XXIII:2 and with Article 6 DSU.³⁰ Canada, on 14 September 1995, requested the

²²Unless otherwise stated, "GATT" Article (number of article) means Article (number of article) of the "GATT 1994".

²³WT/DS8/1.

²⁴A request by the U.S., WT/DS8/2.

²⁵A request by Canada, WT/DS8/3.

²⁶Japan's adoption of the request, WT/DS10/4.

²⁷WT/DS10/1.

²⁸WT/DS10/2; WT/DS10/4.

²⁹WT/DS11/1.

³⁰WT/DS8/5; see, the Report on Japan - Alcohol-II, *supra* note 21, para 1.5.

DSB to establish a panel under its standard terms of reference in accordance with Article XXIII and with Articles 4 and 6 DSU.³¹ Furthermore, the United States, on 14 September 1995, requested the DSB to establish a panel under standard terms of reference in accordance with GATT Article XXII:2 and Articles 4 and 6 DSU.³²

On 27 September 1995, the DSB established a single panel,³³ pursuant to Article 9 DSU,³⁴ to examine the first request of all three complaining parties which related to the same matter.

Claims of the parties

The claims made by the EC were:

The Liquor Tax Law violates GATT Article III:2, first sentence, by applying a higher tax rate on the category of spirits than on each of the two like products, i.e. the two sub-categories of shochu, because "spirits" [particularly, vodka, gin, (white) rum, genever] are like products to the two categories of shochu; alternatively, if all or some of the liquors falling within the spirits mentioned above were found by the Panel not to be like products to shochu within the meaning of the first sentence of Article III:2, the Liquor Tax Law violates Article III:2, second sentence, by applying a higher tax rate on all or some of the liquors falling within the category of spirits than on each of the two directly competitive and substitutable products, the two sub-categories of shochu; and further,

the Liquor Tax Law violates GATT Article III:2, second sentence, by applying a higher tax rates on the categories of whisky/brandy and liqueurs than on each of the two sub-categories of shochu, since whisky/brandy and liqueurs are "directly competitive and substitutable products" to both categories of "shochu". (para. 3.1)

The claims made by Canada were:

Whisky is a "directly competitive and substitutable product" to both categories of "shochu", and by applying a higher tax rate on the categories of whisky/brandy than on each of the two sub-categories of shochu, the Liquor Tax Law distorts the relative prices of whisky and shochu, and in so doing the Liquor Tax Law distorts consumer choice between these categories of alcoholic beverages and therefore distorts their competitive relationship. Accordingly,

³¹WT/DS10/5; see *ibid.*, para. 1. 6

³²WT/DS11/2; see *ibid.*, para. 7.

³³The Panel was constituted on 30 October 1995. [Panel members: Mr. Hardeep Puri (Chairman); Mr. Luzius Wasescha and Mr. Hugh McPhail (Panellists)], see *ibid.*, para. 11.

³⁴*Ibid.*, para. 1.8; WT/DS/M/7.

the Liquor Tax Law is inconsistent with GATT Article III:2, second sentence. (para. 3.2)

The claims made by the United States were:

The Japanese tax system applicable to distilled spirits has been devised so as to afford protection to the production of shochu. In addition, since "white spirits" and "brown spirits" have similar physical characteristics and end-uses, the US claimed that "white spirits" and "brown spirits" are "like products" as defined in the first sentence of Article III:2, and thus the difference in tax treatment between shochu and vodka, rum, gin, other "white spirits", whisky/brandy and other "brown spirits" is inconsistent with Article III:2, first sentence;

If this is not the case, alternatively, the Panel find that all "white spirits" are "like products" in the sense of Article III:2 first sentence, and all distilled spirits are "directly competitive and substitutable" in terms of Article III:2, second sentence for the same reason; therefore, the Liquor Tax Law should be found to be inconsistent with Article III:2. (para. 3.3)

With respect to those claims from the three complaining parties, Japan replied:

-The purpose of the tax classification pursuant to the Liquor Tax Law is not to afford protection and also not to have the effect of protecting domestic production. The Liquor Tax Law, therefore, does not violate Article III:2;

-Spirits, whisky/brandy and liqueurs are not "like products" to either category of shochu, within the meaning of GATT Article III:2, first sentence, nor are they "directly competitive and substitutable products" to shochu, within the meaning of Article III:2, second sentence;

According to the above reasons, the Liquor Tax Law cannot violate Article III:2;

-In the meantime, Japan requests the Panel to turn down the claim of the US with respect to Japan's Taxation Special Measures Law because it is not mentioned in the terms of reference of the Panel. (para. 3.4)

Summary of Findings and Conclusions:

The Preliminary Finding:

With respect to the U.S. claim concerning the Japanese Taxation Special Measures Law, the Panel concluded that its terms of reference did not permit to consider this claim (Articles 7 and 11 DSU).³⁵ The Panel further noted that the Japanese Taxation Special Measures Law is not referred to in any of those documents mentioned. Accordingly, the Panel concluded that the U.S. claim with respect to the Japanese Taxation Special Measures Law is not permitted under the terms of reference and therefore, the Panel merely examines the other claims. (para. 6.5)

³⁵WT/D8/6, WT/DS10/6 and WT/DS11/3.

The Panel noted that the main claim of the complainants was that the Liquor Tax Law was inconsistent with GATT Article III:2. To examine this complaint, the Panel referred to Article III:2,³⁶ Article III:1,³⁷ and an Interpretative Note Ad Article III, Paragraph 2,³⁸ contained in Annex I to GATT 1994.³⁹ In addition, with respect to the Interpretative Note Ad Article III, Paragraph 2, the Panel noted that "the annexes to this Agreement are hereby made an integral part of this Agreement" as provided in GATT Article XXXIV.

The Main Findings:

1. General Principles of Interpretation

For resolving the dispute over the appropriate legal analysis to be applied, the Panel was required to interpret the wording of GATT Article III:2. The Panel recalled that Article 3:2 DSU stated:

...The Members recognise that [the WTO dispute settlement system] serves to preserve the rights and obligations of Members under the covered agreements,

³⁶See, Appendix IV of the thesis.

GATT Article III:2 provides that:

The products of the territory of any contracting party imported into the territory of any other contracting party shall not be subject, directly or indirectly, to internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly, to like domestic products. Moreover, no contracting party shall otherwise apply internal taxes or other internal charges to imported or domestic products in a manner contrary to the principles set forth in paragraph 1.*

[*The paragraph with the asterisk should be read in conjunction with Annex I (Notes and Supplementary Provisions) of the General Agreement. Therefore, in reading this Article, the Interpretative Note ad Article III, Paragraph 2 should be referred to].

³⁷*Ibid.*

GATT Article III:1 provides that:

The contracting parties recognise that internal taxes and other internal charges, and laws, regulations and requirements affecting the internal sale, offering quantitative regulations requiring the mixture, processing or use of products in specified amounts or proportions, should not be applied to imported or domestic products so as to afford protection to domestic production.*

[Although this Article refers to the Interpretative Note ad Article III, Paragraph 1, it is not presented here because of its irrelevancy to this case.]

³⁸*Ibid.*

Interpretative Note Ad Article III, Paragraph 2 provides that:

A tax conforming to the requirements of the first sentence of paragraph 2 would be considered to be inconsistent with the provisions of the second sentence only in cases where competition was involved between, on the one hand, the taxed product and, on the other hand, a directly competitive or substitutable products which was not similarly taxed.

³⁹*Supra* note 21, para. 6.6.

and to clarify the existing provisions of those agreements in accordance with customary rules of interpretation of public international law.

The Panel mentioned that the "customary rules of interpretation of public international law" indicated above were incorporated in the Vienna Convention on the Law of Treaties (hereinafter, the "VCLT");⁴⁰ The Panel further noted that Article 3:2 DSU actually codified the practice previously established; The Panel understood that Articles 31 and 32 VCLT⁴¹ gave the relevant criteria from the aspect of how Article III:2 should be interpreted in this case; The Panel concluded that the starting point of interpreting of an international treaty such as the GATT 1994 was the wording of the treaty (in accordance with Article 31 VCLT). (para. 6.9)

⁴⁰*Ibid.*, para. 6.7.; Prior to this case, the Panel has already interpreted the GATT pursuant to the VCLT. For example, see *ibid.*, *supra* note 21, para. 6.7 as footnote 81, the Report on Japan - Alcohol-I, *supra* note 21; the panel report on EC - Imposition of Anti-dumping Duties on Imports of Cotton Yarn From Brazil, ADP/137, adopted on 30 October 1995, paras. 540ff.; the AB report on United States - Standards for Reformulated and Conventional Gasoline, WT/DS2/AB/R, adopted on 20 May 1996.

⁴¹Article 31 (General rule of interpretation) of the Vienna Convention on the Law of Treaties (VCLT) provides that:

1. A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.
2. The context for the purpose of the interpretation of a treaty shall comprise, in addition to the text, including its preamble and annexes:
 - (a) any agreement relating to the treaty which was made between all the parties in connection with the conclusion of the treaty;
 - (b) any instrument which was made by one or more parties in connection with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.
3. There shall be taken into account together with the context:
 - (a) any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions;
 - (b) any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation;
 - (c) any relevant rules of international law applicable in the relations between the parties.
4. A special meaning shall be given to a term if it is established that the parties so intended.

Article 32 (Supplementary means of interpretation) of the VCLT provides that:

- Recourse may be had to supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion, in order to confirm the meaning resulting from the application of article 31, or to determine the meaning when the interpretation according to article 31:
- (a) leaves the meaning ambiguous or obscure; or
 - (b) leads to a result which is manifestly absurd or unreasonable.

Article 1(b)(iv) of GATT 1994 provides institutional recognition of the principle that adopted panel reports constitute subsequent practice; the Panel was of the view that panel reports adopted by the CPs constitute subsequent practice in specific cases, and, as such, have to be taken into account by subsequent panels dealing with the same or a similar issue; the Panel, however, noted that it does not necessarily have to follow their reasoning or results; the Panel further noted that unadopted panel reports have no legal status in the GATT and WTO system since they have not been endorsed through decisions made by the CPs regarding GATT or WTO Members. (para. 6.10)

2. Article III

According to the Panel, Article III:2 deals with two different factual situations: Article III:2, first sentence is about the treatment of "like products", while Article III:2, second sentence deals with the treatment of "directly competitive or substitutable products". In addition, the Interpretative Note Ad Article III:2 further spells out this distinction and confirms the two distinct obligations prescribed in Article III:2.

The Panel noticed that Article III:1 covers general principles with respect to the imposition of internal taxes, internal charges, and laws, regulations and requirements affecting the treatment of imported and domestic products, while Article III:2 refers to specific obligations concerning internal taxes and internal charges; Furthermore, the words used in Article III:1, such as "recognise" and "should" as well as the word in Article III:2, second sentence, "the principles", confirms that Article III:1 does not contain a legally binding obligation but rather states general principles; On the other hand, the wording "shall" in Article III:2, both sentences, clarifies that Article III:2 contains two legally binding obligations; Accordingly, the starting point for an interpretation of Article III:2 is Article III:2 itself and not Article III:1. If it is relevant and necessary, reference to Article III:1 (constituting part of the context of Article III:2) will be made. (para. 6.12)

The Panel then referred to other contextual elements that had to be taken into account, as required by Article 31 VCLT in light of the relationship between Article II and III; The Panel concluded, as had previous panels that dealt with the same issue,⁴² that one of the main purpose of Article III is to guarantee that WTO Members will not undermine through internal measures their commitments under Article II. (para. 6.13)

3. Article III:2, First Sentence

With respect to like products, the Panel noted that the Community essentially argued in favour of a two-step procedure, namely, the Panel should establish first whether the products in question are like, and, if so, then proceed to examine whether taxes imposed on foreign products are in excess of those imposed on like domestic products; The Community had stated that physical characteristics of the products concerned, their end-uses, as well as consumer preferences could provide relevant criteria for the Panel to judge whether the products concerned were like; The Panel further noted in this respect, that complainants have the burden of proof to demonstrate first, that products are like and second, that foreign products are taxed in excess of domestic ones. (para. 6.14)

Furthermore, the Panel commented on the Japanese statements that essentially argued in favour of the contested legislation concerning its aims and effect in order to determine whether or not it was consistent with Article III:2; According to this view, in this case the aims and effect of the contested legislation did not operate so as to afford protection to domestic production, and no inconsistency with Article III:2

⁴²Moreover, the Panel added to this point by citing the adopted panel report which had stated that "*...one of the basic purpose of Article III was to ensure that the contracting parties' internal charges and regulations were not such as to frustrate the effect of tariff concessions granted under Article II...*" (The panel report on "Canada - Import, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies", adopted on 18 February 1992, BISD 39S/27, paras. 5.30-5.31.); in another adopted panel report, the panel remarked that "*...the most-favoured-nation requirement in Article I, and also tariff bindings under Article II, would become ineffective without the complementary prohibition in Article III on the use of internal taxation and regulation as a discriminatory non-tariff trade barrier*" (The panel report on "United States - Measures Affecting Alcoholic and Malt Beverage" (U.S. - Malt Beverages), adopted on 19 June 1992, BISD 39S/206, para. 5.9; see also, para. 6.21.).

could be established; In addition to this statement by Japan, the U.S. argued that, in determining whether two products that were taxed differently were 'like products' for the purpose of Article III:2, the Panel should examine not only the similarity in physical characteristics and end-users, consumer tastes and preferences, and classification of tariff for each product but also whether the tax distinction in question was "applied ... so as to afford protection to domestic production". (para. 6.15)

The Panel noted that the proposed aim-and-effect test was inconsistent with the wording of Article III:2, first sentence; The Panel noted that Article III:2, first sentence, contained no reference to those words; The Panel noted that the complainants, according to the aim-and-effect test, would have the burden of showing not only the effect of a particular measure, which was in principle discernible, but also its aim, which was sometimes indiscernible; The Panel did not accept the argument by the U.S. that the aim-and-effect test should be applicable only with respect to origin-neutral measures; The Panel noted that neither the wording of Article III:2, nor that of Article III:1 supported a distinction between origin-neutral and origin-specific measures. (para. 6.16)

The Panel further noted that the list of exceptions contained in GATT Article XX could become redundant or useless because the aim-and-effect test did not contain a definitive list of grounds justifying departure from the obligations that were otherwise incorporated in Article III; In principle, a WTO Member could, for example, invoke protection of health in the context of involving the aim-and-effect test; The Panel noted that if this were the case, then the standard of proof established in Article XX would effectively be circumvented; WTO Members would not have to prove that a health measure was 'necessary' to achieve its health objectives. (para. 6.17)

The Panel touched upon two GATT panel reports which referred to the aim-and-effect test; In the Panel report on "United States - Taxes on Automobiles

(US - Auto Taxes)"⁴³, the Panel stated that the report remained unadopted and therefore did not have to take it into account because it did not constitute subsequent practice⁴⁴; With respect to the U.S. - Malt Beverages case, the Panel made reference to the fact that its interpretation of "like products" (Article III:2) was largely consistent with the interpretation of the 1987 Panel Report; In the 1992 Malt Beverages report, the Panel took into account the product's end-uses, consumer tastes and habits, and the product's properties, nature and quality when it interpreted "like products"; In addition, that report also considered whether product differentiation was being used "so as to afford protection to domestic production";⁴⁵ The Panel finally decided not to follow the interpretation of "like product" in Article III:2, first sentence, supported by the U.S. - Malt Beverage report in so far as it incorporated the aim-and-effect test. (para. 6.18)

The Panel, having decided not to apply the aim-and-effect test proceeded to develop the legal tests which it would apply in this case in order to determine whether Japan had acted inconsistently with its obligations under Article III; In addition, more specifically, the Panel considered the wording of Article III:2, first sentence, which required it to examine three points: (i) whether the products at issue are like, (ii) whether the contested measure is an "internal tax" or "other internal charge" (this was not an issue in this case) and (iii) if so, whether the tax imposed on foreign products is in excess of the tax imposed on like domestic products; If those three tests resulted in the affirmative, such a tax would result in the WTO Members holding it to be in violation of obligations under Article III:2, first sentence; The Panel further stated that past GATT panels had followed this approach.⁴⁶

i) "Like Products"

The Panel noted that the term 'like product' appears in various GATT provisions, and thus the interpretation of this term varies; In this respect, the Panel referred to the

⁴³DS31/R (11 October 1994) which is unadopted.

⁴⁴*Ibid.*, *supra* note 21, para. 6.10.

⁴⁵The Report on U.S. - Malt Beverages, *supra* note 42, paras. 5.25-5.26.

⁴⁶See footnote 94 in the Report on Japan - Alcohol-II, *supra* note 21.

discrepancy between Article III:2 and III:4, namely, the former referred to Article III:1 and to "like", as well as to directly competitive or substitutable products (see Article XIX), whereas the latter referred merely to like products. (para. 6.20)

The Panel noted that previous Panel and working party reports had unanimously agreed that the term 'like product' should be interpreted on a case-by-case basis; To establish likeness, previous Panels had used different criteria, such as the products' properties, nature and quality, and its end-uses; consumers' tastes and habits, which varied from country to country as well as the product's definition under tariff nomenclatures; The Panel viewed that 'like products' need not be identical in all respects; However, that term should be construed narrowly in the case of Article III:2, first sentence; This approach was dictated by two independent reasons: (i) Article III:2 distinguishes between "like" and "directly competitive or substitutable" products, the latter obviously being a much larger category of products than the former; and (ii) the Panel's conclusions arrived at with respect to the relationship between Articles III and II; As to the second point, as previous panels had noted, one of the main objectives of Article III:2 is to ensure that WTO Members do not frustrate the effect of tariff concessions granted under Article II through internal taxes and other internal charges. It followed that a parallel required to be drawn in this case between the definition of products for the purpose of Article II tariff concessions and the term 'like product' as it appeared in Article III:2; This is so in the Panel's view, because with respect to two products subject to the same binding tariff and therefore subject to the same maximum border tax, there was no justification, outside of those stipulated in GATT rules, to tax them in a different manner through internal taxation; In the Panel's view, especially where it was in sufficient detail, a product's description used for this purpose was an important criterion for confirming likeness for the purpose of Article III:2. (para. 6.21)

The Panel then stated its conclusions concerning the relationship between Articles II and III; In this context, it noted that (i) vodka and shochu had been classified under the same heading in the Japanese tariffs; and (ii) vodka and shochu were covered by

the same Japanese tariff were at the time of its negotiations; the Panel concluded that vodka and shochu were like products; besides, substantial noticeable differences in physical characteristics existed between the rest of the alcoholic beverages in dispute and shochu which disqualified them from being regarded as like products; more specifically, the use of additives disqualified liqueurs, gin and genever; the use of ingredients disqualified rum; lastly, appearance (arising from manufacturing processes) disqualified whisky and brandy; the Panel therefore decided to examine whether the rest of the alcoholic beverages, other than vodka, could qualify as products directly competitive or substitutable to shochu. (para. 6.23).

With respect to the question whether the products, in particular, vodka and shochu, at issue in this case were like products, the Panel essentially followed the same conclusion which had been reached in the 1987 Panel Report;⁴⁷ The Panel expressed its view that vodka and shochu shared most physical characteristics, though noted a difference in the physical characteristics of alcoholic strength between the two products; Despite that fact, the Panel did not preclude a finding of likeness especially since alcoholic beverages are often consumed in diluted form; The Panel then moved on to the issue concerning the relationship between Articles II and III. With respect to vodka, the Panel noted that Japan offered no further convincing evidence that the 1987 Panel Report reached the wrong conclusion; The Panel also noted that Japan's basic argument was not that the two products, i.e. shochu and vodka, are unlike, in terms of the criteria applied in 1987, but rather that they were unlike because the Japanese tax legislation did not have the aim and effect of protecting shochu; Nonetheless, as referred to earlier on, the Panel had already refused to apply the

⁴⁷The Report on Japan - Alcohol-I, *supra* note 21, para. 5.7 stated that "...agreed with the arguments submitted to it by the European Communities, Finland, and the United States that Japanese shochu (Group A) and vodka could be considered as 'like' products in terms of Article III:2 because they were both white/clean spirits, made of similar raw materials, and the end-uses were virtually identical".

"...the Panel found that the traditional Japanese consumer habits with regard to shochu provided no reason for not considering vodka to be a 'like' product. ...Even if imported alcoholic beverages (e.g. vodka) were not considered to be 'like' to Japanese alcoholic beverages (e.g. shochu Group A), the flexibility in the use of alcoholic drinks and their common characteristics often offered an alternative choice for consumers leading to a competitive relationship".

aim-and-effect test; In the end, the Panel concluded that vodka and shochu were like products; According to the Panel, only vodka could be considered as a like product to shochu since they shared the most physical characteristics; The only difference was the means employed for filtration. There were substantially noticeable differences in the physical characteristics between the rest of the alcoholic beverages in dispute and shochu, which disqualified them from being regarded as like products; Accordingly, the Panel decided to examine whether the alcoholic beverages, excluding vodka, could qualify as directly competitive or substitutable products to shochu; In fact, the 1987 Panel Report has also considered this point regarding these products but only with respect to the question under Article III:2, second sentence.

ii) "Taxation in Excess of those on Like Domestic Products"

The Panel then examined whether vodka was taxed higher than shochu under the Liquor Tax Law; the phrase "not in excess of those applied to like domestic products" should be understood to mean at least identical or better tax treatment. Since the Japanese tax was calculated on the basis of and varied according to the alcoholic content of the product, the taxes imposed on vodka (i.e. 9,927 Yen per degree of alcohol) were obviously higher than those imposed on shochu (i.e. 6,228 Yen per degree of alcohol). The Panel, therefore, concluded that the tax imposed on vodka was in excess of the tax imposed on shochu. (para. 6.24)

The Panel addressed the Japanese argument that its legislation, by keeping the tax/price ratio 'roughly constant', was trade neutral and consequently no protective aim and effect of the legislation could be detected. In this connection, the Panel considered Japan's argument that its aim was to achieve neutrality and horizontal tax equity; The Panel noted that it had already decided that the existence or non-existence of a protective aim and effect was irrelevant in an analysis under Article III:2, first sentence. Eventually, the Panel rejected Japan's argument [i.e. the Liquor Tax Law did not impose on foreign products a tax in excess of the tax imposed on domestic like products for the following reasons:

"(i) Essentially, in the context of Article III:2, first sentence, it is irrelevant whether 'roughly' the same treatment through, for instance, a 'roughly constant'

tax/price ratio is afforded to domestic and foreign like products or whether neutrality and horizontal tax equity is achieved;

"(ii) There were significant problems with the methodology for calculating tax/price ratios submitted by Japan, such that arguments based on that methodology could only be viewed as inconclusive. More particularly, although Japan had argued that the comparison of tax/price ratios should be done on a category-by-category basis, its statistics on which the tax/price ratios were based excluded domestically produced spirits from the calculation of tax/price ratios for spirits and whisky/brandy. Since, the prices of the domestic spirits and whisky/brandy are much lower than those of the imported goods, this exclusion has the impact of reducing considerably the tax/price ratios specified by Japan for those products. In this connection, the Panel noted that one consequence of the Japanese tax system was to make it more difficult for cheaper imported brands of spirits and whisky/brandy to enter the Japanese market. In addition, the Panel noted that the Japanese statistics were based on suggested retail prices and there was evidence in the record that these products were often sold at a discount at least in Tokyo. To the extent that the prices were unreliable, the resultant tax/price ratios would be unreliable as well;

"(iii) The legislation contested did not refer to its purpose that it was to maintain a 'roughly constant' tax/price ratio. This was rather an *ex post facto* rationalisation by Japan, and there are no guarantees in the legislation that the tax/price ratio will always be maintained 'roughly constant'". (para. 6.25)

The Panel then turned to the arguments put forward by Japan concerning taxation systems in other country. The Panel noted that there has been only one instance of adjustment since the modification of Japan's Liquor Tax Law in 1989. Despite Japan's arguments concerning taxation systems in other countries, the Panel noted that its terms of reference in this case were strictly limited to Japanese legislation.⁴⁸ Consequently, the Panel concluded that, by taxing vodka in excess of shochu, Japan violated its obligation under Article III:2, first sentence.⁴⁹

4. Article III:2, Second Sentence

i) "Directly Competitive or Substitutable Products"

In the view of the Panel, Article III:2, second sentence require it to make two determination: (i) whether the products concerned (whisky, brandy, gin, genever, rum and liqueurs) were directly competitive or substitutable, and (ii) if so, whether the

⁴⁸*Ibid.*, para. 6.26.

⁴⁹*Ibid.*, para. 6.27.

treatment afforded to foreign products was contrary to the principles set forth in paragraph 1 of Article III. In the view of the Panel, the complainants had the burden of proof to demonstrate first, that the products concerned were directly competitive or substitutable and second, that foreign products were taxed in such a way so as to afford protection to domestic production; the Panel decided that the term 'directly competitive or substitutable product', in accordance with its ordinary meaning, should be interpreted more broadly than the term 'like product'. In this respect the Interpretative Note Ad Article III:2, second sentence refers to products 'where competition was involved between...' them. In this respect, the Panel noted that independent of similarities with respect to physical characteristics or classification in tariff nomenclatures, greater emphasis should be placed on elasticity of substitution. The Panel noted the conclusions in the 1987 Panel Report⁵⁰ (i.e. a tax system that discriminates against imports has the consequence of creating and even freezing preference for domestic goods. In the Panel's view, this meant that consumer surveys in a country with such a tax system would likely understate the degree of potential competitiveness between substitutable products. (para. 6.28)

With respect to the evidence lodged in this case, the Panel noted that the complainants had submitted a study (the ASI study) that concluded that there was a high degree of price-elasticity between shochu, on the one hand, and five brown spirits (Scotch whisky, Japanese whisky, Japanese brandy, cognac, and North American whisky) and three white spirits (gin, vodka and rum), on the other. Japan questioned the relevance of this ASI study by noting that consumers were not allowed to choose other than the eight products mentioned above (for example, they were not allowed to choose beer, sake or wine) and also argued that if choices were too limited even such disparate products as hamburger and ice cream could be regarded as being directly competitive or substitutable products. In the Panel's view, however, price-elasticity between the products mentioned was not altered by the fact that consumers were presented with a limited choice. At best, the Japanese argument, if proven, could ultimately lead to the conclusion that the three products

⁵⁰*Ibid.*, para. 5.9.

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mentioned by Japan had a greater degree of price-elasticity in relation to shochu. It would not, however, in the Panel's view, amount to a rejection of the existence of a significant directly competitive or substitutable relationship between shochu and the examined eight products. (para. 6.29)

The Panel further noted that the distinction between "premium whisky", "first grade whisky" and "second grade whisky" was abolished as a result of the 1989 Japanese tax reforms. This tax reform disadvantaged domestically produced whisky, by substantially increasing the tax rate on second grade whisky compared to the other alcoholic beverages at issue in the present case. The market share of domestic whisky including second grade fell from 26.7 percent in 1988 to 19.6 percent in 1990. This proved to the Community that there was elasticity of substitution between whisky and shochu. The Panel took note in its response, Japan's argument that a combination of an expansion of shochu consumption and declining whisky prices tended to indicate a lack of competitive relationship between the two commodities. In the Panel's view, Japan failed to take account of the fact that shochu and foreign whisky were in fact capturing the market share lost by domestically produced whisky. In the Panel's view, the fact that foreign produced whisky and shochu were competing for the same market was evidence that there was elasticity of substitution between them. (para. 6.30)

The Panel noted Japan's argument that there was no elasticity of substitution between shochu and the rest of the alcoholic drinks in dispute in this case; Japan based its argument on a survey conducted among consumers that showed, according to Japan, that if shochu was not available, 6 percent of consumers would switch to spirits, whereas only 4 percent would switch to whisky; if whisky was not available, 32 percent of consumers would choose brandy and only 10 percent would choose shochu. Japan submitted this survey to the Panel. The Panel did not accept Japan's argument on the grounds that Japan, in conducting this survey, failed to take into account price distortions caused by internal taxation. In other words, consumers would switch to spirits and whisky. This, in the Panel's view, was proof of

significant elasticity of substitution between shochu, on the one hand, and whisky and spirits, on the other. (para 6.31)

The Panel concluded by adding that whether shochu and the other products in dispute were directly competitive or substitutable products, it was notable that the products concerned were all distilled spirits and it would give particular emphasis to factors such as: the findings of the 1987 Panel Report; the ASI studies submitted by the complainants (this study demonstrated persuasive evidence that there was significant elasticity of substitution among the products in dispute); the survey submitted by Japan, notwithstanding the fact that it failed to take into account price distortions caused by internal taxation, but, nonetheless, illustrated elasticity of substitution among the products in dispute; and, the evidence submitted by the complainants concerning the 1989 Japanese tax reform, which indicated that whisky and shochu were essentially competing for the same market. In the view of the Panel, the conclusions of the 1987 Panel Report, buttressed by any of the other three factors, were sufficient for the Panel to conclude that shochu and the other products subject of the dispute were directly competitive or substitutable under Article III:2, second sentence. (para. 6.32)

ii) "So as to Afford Protection"

In the Panel's view, if directly competitive or substitutable products were not 'similarly taxed', and if it were found that the tax favoured domestic products, then protection would be afforded to such products, and Article III:2, second sentence was violated; Although the 1987 Panel Report did not focus on the Interpretative Note Ad Article III, its conclusion on the issue of 'so as to afford protection' was essentially the same, as it concluded that higher (i.e. dissimilar) Japanese taxes on imported alcoholic beverages and the existence of substitutability were 'sufficient evidence of fiscal distortions of the competitive relationship between imported distilled liquors and domestic shochu affording protection to domestic producers of shochu';⁵¹ The Panel agreed with this conclusion. In this connection, the Panel noted that for it to

⁵¹*Ibid.*, at para. 5.11.

conclude that dissimilarity in taxation afforded protection, it would be sufficient for it to uphold this view to find that the dissimilarity in taxation was not *de minimis*; The Panel took the view that it was appropriate to conclude, as have other GATT panels including the 1987 panel, that it was not necessary to demonstrate any adverse effect on the level of imports, as Article III generally was aimed at providing imports with 'effective equality of opportunities' in 'conditions of competition'.⁵² In line with these interpretations of Article III, the Panel concluded that it was not necessary for the complainants to establish the purpose or aim of tax legislation in order for the Panel to conclude that dissimilar taxation afforded protection to domestic production; In the Panel's view, the following indicators were relevant in determining whether the products in dispute were similarly taxed in this case: tax per litre of product, tax per degree of alcohol, *ad valorem* taxation, and the tax/price ratio.

- a. With respect to taxation per kilolitre of product, the Panel concluded that the amounts of tax were not similar and that the differences were not *de minimis*.

Shochu A (25°) ¥ 155,700
 Shochu B (25°) ¥ 102,100
 Whisky (40°) ¥ 982,300
 Brandy (40°) ¥ 982,300
 Spirits (38°) ¥ 377,230 (gin, rum, vodka)
 Liqueurs (40°) ¥ 328,760

- b. With respect to taxation per degree of alcohol, the Panel concluded that the amounts of tax were not similar and that differences were not *de minimis*.

Shochu A (25°) ¥ 6,228
 Shochu B (25°) ¥ 4,084
 Whisky (40°) ¥ 24,558
 Brandy (40°) ¥ 24,558
 Spirits (38°) ¥ 9,927 (gin, rum, vodka)
 Liqueurs (40°) ¥ 8,219

- c. The Panel noted that Japan's Liquor Tax Law did not provide for *ad valorem* taxation and this criterion was, consequently, irrelevant in this case.

- d. With respect to the tax/price ratio, the Panel noted that the statistics submitted by Japan showed that significant differences existed between shochu and the other directly competitive or substitutable products and also noted that

⁵²See, for example, the U.S. - Taxes on Petroleum and Certain Imported Substances (U.S. - Superfund), **BISD 39S/206** at para. 5.6.; the Panel Report on "Italian Discrimination Against Imported Agricultural Machinery", **BISD 7S/23** (1959), adopted on 23 October 1958, para. 12.

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there were significantly different tax/price ratios within the same product categories.

The Panel consequently concluded that the products in dispute were not similarly taxed and that taxes on shochu were lower than the taxes imposed on the other products subject to dispute, leading the Panel to the conclusion that protection was afforded to shochu inconsistent with Japan's obligations under Article III:2, second sentence. (para. 6.33)

In the Panel's view, the argument brought by Japan that its legislation, in keeping the tax/price ratio 'roughly constant' was trade neutral and did not operate 'so as to afford protection to domestic protection', should be rejected. (para. 6.34)

The Panel accepted the evidence submitted by Japan, according to which a shochu-like product was produced in various countries outside Japan, including the Republic of Korea, the People's Republic of China and Singapore; the Panel noted, however, that Japanese import duties on shochu were set at 17.9 percent; At any rate what was at stake, in the Panel's view, was the market share of the domestic shochu market in Japan that was occupied by Japanese-made shochu; the Panel took the view that the combination of custom duties and internal taxation in Japan had the following impact: on the one hand, it made it difficult for foreign-produced shochu to penetrate the Japanese market and, on the other hand, it did not guarantee equality of competitive conditions between shochu and the rest of the "white" and "brown" spirits. (para. 6.35)

The Panel reached the conclusions:

-Shochu and vodka were 'like products' and Japan, by taxing the latter in excess of the former, was in violation of its obligation under GATT Article III:2, first sentence.

-Shochu, whisky, brandy, rum, gin, genever, and liqueurs were 'directly competitive or substitutable products' and Japan, by not taxing them similarly,

was in violation of its obligation under GATT Article III:2, second sentence.
(paras. 71-72)

The Panel recommended that the DSB request Japan to bring its Liquor Tax Law into conformity with its obligations under the GATT 1994.

8.1.2.1.2. Report of the Appellate Body⁵³

As explained earlier, the function of the Appellate Body ("AB") can be defined as to ensure the predictability and transparency of dispute procedures by means of improving coherence of panel reports. For that reason, as stipulated in Article 17:6 DSU, the scope of the AB is limited to legal issues contained in the panel report and legal interpretations arrived at by the panel. Up to now, Members are actively utilising this appellate service.⁵⁴

Summary of Arguments of Participants:

In this appeal, Japan and the U.S. were both an appellant /appellee, while Canada and the EC were an appellee. The appeal was initiated pursuant to the Working Procedures for Appellate Review (hereinafter, the "Working Procedures"):⁵⁵

"On 8 August 1996, Japan notified the DSB of the WTO of its decision to appeal certain issues of law covered in the Panel Report and legal interpretations developed by the Panel (para. 4 of Article 16 DSU), and filed a Notice of Appeal with the Appellate Body (Rule 20 Working Procedures [Commence of Appeal]); then, on 23 August 1996, the U.S. filed an appellant's submission (Rule 23(1) Working Procedures [Multiple Appeals]); and, on 2 September 1996, the E.C., Canada and the U.S. submitted an appellees' submission (Rule 22 Working Procedures [Appellee's Submission]), and on

⁵³Report of the AB on Japan - Alcohol-II, WT/DS8/AB/R; WT/DS10/AB/R; WT/DS11/AB/R (4 October 1996). The members of the AB in this case were: Julio Lacarte-Muró (Presiding Member); James Bacchus; Said El-Naggar.

⁵⁴As of 3 November 1998, there are only three cases which have not been appealed, that is, the Japan - Film case (WT/DS44), the Indonesian National Car case (WT/DS54, 55, 59 and 64) and the India Patent case (complained by EC) (WT/DS79).

⁵⁵WT/AB/WP/1(15 February 1996), which was consolidated, revised and replaced by WT/AB/WP/3 (28 February 1997).

that same day, Japan submitted an appellee's submission (Rule 23(3) Working Procedures [Multiple Appeals])".⁵⁶

All the participants submitted their respective arguments in the appeal.

1. Japan:

Apart from arguments concerning the Panel's errors which are listed below, Japan responded by stating that the U.S.'s arguments were not based on a correct understanding of the Japanese liquor tax system, namely, the Liquor Tax Law, which had the legitimate policy purpose of ensuring neutrality and equity, in particular, horizontal equity, and it had neither the aim nor the effect of protecting domestic production. Japan asserted that it was incorrect to conclude that all distilled liquors were "like products" (Article III:2, first sentence), or to conclude that the Liquor Tax Law was inconsistent with Article III:2 because it imposed a tax on imported distilled liquors in excess of the tax imposed upon like domestic products.

According to Japan, the Panel erred in

- failing to interpret Article III:2, first and second sentences in light of Article III:1;
- disallowing an "aim-and-effect" test to determine whether the Liquor Tax Law was applied "so as to afford protection to domestic production";
- ignoring whether there was "linkage" between the origin of products and the tax treatment they incurred and, in this respect, not comparing the tax treatment of domestic products as a whole and foreign products as a whole under the Liquor Tax Law;
- not giving proper weight to tax/price ratios as a yardstick to compare tax burdens;
- failing to interpret correctly the principle of Article III:1, in particular, the language "so as to afford protection to domestic production", erroneously placing excessive emphasis on the phrase "not similarly taxed" in the Note Ad Article III:2;

⁵⁶See, the Report of the AB on Japan - Alcohol-II, *supra* note 53, at 2.

-placing excessive emphasis on tariff classification in finding that shochu and vodka were "like products" within the meaning of Article III:2, first sentence, arguing that the relevant tariff binding indicated that these products were not "like".

2. United States:

The U.S. supported the Panel's conclusions in general but alleged several errors, as listed below, in the Panel's findings and in the legal interpretations developed by the Panel in drawing its conclusions in its Report. Apart from arguments with respect to the those errors, the U.S. responded to the claims of error pointed out in Japan's (appellant's) submission that: the national treatment provisions (Article III) could apply to origin-neutral measures; Japan's taxation under the Liquor Tax Law had the aim and effect of affording protection to domestic production; and the tax/price ratios quoted by Japan were not the appropriate basis for evaluating the consistency of taxation under the Liquor Tax Law with Article III:2.

According to the U. S., the Panel erred in

- disregarding Article III:1, which the U.S. saw as an integral part of the context that must be considered in interpreting Article III:2, and Article III generally;
- not finding that all distilled spirits constituted "like products" under Article III:2, first sentence;
- drawing a connection between national treatment obligations and tariff bindings;
- interpreting the term "directly competitive or substitutable products" provided for in the Ad Article to the second sentence of Article III:2 by not considering whether a tax distinction was applied "in a manner contrary to the principles set forth in Article III, paragraph 1", that is, "so as to afford protection to domestic production";
- using cross-price elasticity as the "decisive criterion" for whether products were "directly competitive or substitutable";

-not addressing the full scope of the products subject to the dispute in that there was inconsistency between the Panel's conclusions on "directly competitive or substitutable products" (para. 7.1 (ii) of the Panel Report) and the conclusions (paras. 6.23-6.33 of the Panel Report);

-incorrectly assessing the relationship between Article III:2 and Article III:4 by stating that the product coverage of the two provisions was not identical; and

-incorrectly characterising adopted panel reports as "subsequent practice" within the meaning of Article 31(3)(b) of the VCLT.

3. European Communities:

a. Article III:2, first sentence

The EC supported the Panel's conclusions, especially the Panel's rejection of the "aim-and-effects" test with respect to the interpretations of Article III, first and second sentences. The EC also supported the Panel's holding that the essential criterion for a "like product" determination was similarity of physical characteristics and that tariff nomenclatures might be relevant for a determination of "likeness". Nonetheless, the EC was not entirely satisfied with the Panel's conclusions regarding the range of products found to be "like" under Article III:2, first sentence, namely, the EC claimed that those conclusions primarily involved an assessment of facts and, thus, were not reviewable by the AB, which was limited to the consideration of issues of law under Article 17:6 DSU.

b. Article III:2, second sentence

The EC asserted that Japan's argument, i.e. the Liquor Tax Law was not applied "so as to afford protection to domestic production" of shochu because shochu was also produced in other countries and, thus, was not an "inherently domestic product" resulted in two wrong propositions: (i) that "domestic production" of shochu was not "protected" if the same tax treatment was accorded to foreign shochu; and, (ii) the mere fact that shochu was produced in third countries was sufficient to conclude that foreign shochu might benefit from the lower tax as

much as domestic shochu and, consequently, thus protection to production was not afforded only to domestic production.

c. The status of adopted panel reports

The EC concluded that the Panel's characterisation of those adopted panels as "subsequent practice in a specific case" was intrinsically contradictory, since the essence of subsequent practice was that it consisted of a large number of legally relevant events and pronouncements. The EC view was that one adopted panel report "would merely constitute part of a wall of the house that constitutes subsequent practice".⁵⁷ The EC, therefore, asked the AB to modify the Panel's legal terminology regarding this issue.

4. Canada

Canada limited its submission and arguments on appeal to Article III:2, second sentence, that is, Canada supported both the Panel's conclusion that the Liquor Tax Law was inconsistent with Article III:2, second sentence, as well as its interpretation that the phrase "so as to afford protection" in Article III:1 does not require a consideration of both the aim and the effect of a measure to determine whether that measure affords protection to domestic production.

Summary of Conclusions and Recommendations:

The AB referred to errors in law found in the Panel report:

- the Panel erred in law in its conclusion that 'panel reports adopted by the GATT CPs and the DSB of WTO constituted subsequent practice in a specific case by virtue of the decision to adopt them';
- the Panel erred in law in failing to take into account Article III:1 in interpreting Article III:2, first and second sentences;
- the Panel erred in law in limiting its conclusions in paragraph 7.1 (ii) on 'directly competitive or substitutable products' to 'shochu, whisky, brandy, rum,

⁵⁷Section B. 3, *ibid.*

gin, genever, and liqueurs', which was inconsistent with the Panel's Terms of Reference; and

-the Panel erred in law in failing to examine 'so as to afford protection' in Article III:1 as a separate inquiry from 'not similarly taxed' in the Ad Article to Article III:2, second sentence.

With the modification to the Panel's legal findings and conclusions set out in this report, the AB affirmed the Panel's conclusions that shochu and vodka were like products and that Japan, by taxing imported products in excess of like domestic products, was in violation of its obligations under Article III:2, first sentence of GATT 1994. Moreover, the AB concluded that shochu and the other distilled spirits and liqueurs listed in HS 2208, except vodka, were "directly competitive or substitutable products", and that Japan, in the application of the Liquor Tax Law, did not similarly tax imported and directly competitive or substitutable domestic products and afforded protection to domestic production in violation of Article III:2, second sentence of GATT 1994. The AB recommended that the DSB request Japan to bring the Liquor Tax Law into conformity with its obligations under the GATT 1994.

Remarks on the Case:

i) Treaty Interpretation

In the present case, both the Panel and AB defined the principles of interpretation to be applied in cases under the WTO DS procedures. Articles 31 and 32 of the VCLT are regarded to be the "customary rule of interpretation of public international law" as provided for in Article 3:2 DSU. The AB took the same position in the U.S. - Standards for Reformulated and Conventional Gasoline (hereinafter, the "U.S. - Gasoline case").⁵⁸ The AB stressed the need to achieve such clarification by reference to the fundamental rules of treaty interpretation provided in Article 31(1) of the VCLT. In the U.S. - Gasoline case, the AB noted that "[o]ne of the corollaries of the 'general rule of interpretation' in the VCLT was that interpretation must give

⁵⁸WT/DS2/9 (adopted 20 May 1996).

meaning and effect to all the terms of the treaty. An interpreter is not free to adopt a reading that would result in reducing whole clauses or paragraphs of a treaty to redundancy or inutility".⁵⁹

ii) Status of Adopted Panel Reports

The AB rejected the Panel's decision that adopted reports constituted "subsequent practice" in accordance with the VCLT Article 31(3)(b), i.e. "in a specific case". The basic approach of the Panel, seems to have been the same as that of the AB. Namely, since such a condition was incompatible with the notion of "subsequent practice" as a precedent, the essence of the Panel's decision seems not to have been that adopted panel reports had to be taken into account by subsequent panels dealing with the same or similar issue, but that their legal reasoning or results did not have to be followed by subsequent panels.⁶⁰ It seems that the expression used in the Panel Report in this respect is inappropriate.

Furthermore, it seems to be appropriate that the AB rejected the Panel's legal reasoning regarding the status of the adopted panel reports, i.e., the adopted panel reports constitute "other decisions of the CONTRACTING PARTIES to GATT 1947" for the purposes of the WTO Agreement, Annex 1A, the GATT 1994, para. 1(b)(iv).⁶¹ Nonetheless, no logical reason was given for this decision by the AB. Under the WTO system, as prescribed in Article IX:2 in the WTO Agreement, it is clear that the Ministerial Conference and the General Council have exclusive authority to interpret the WTO Agreement and the Multilateral Trade Agreements. From this, it is sufficient to conclude that such authority does not exist by implication or by inadvertence elsewhere, whereas, under the GATT 1947, panel reports were adopted by the Council (which was as being equivalent to the CONTRACTING PARTIES). According to the report by the AB, it said that "a decision to adopt a panel report did not under GATT 1947 constitute agreement by the CONTRACTING PARTIES on the legal reasoning contained in that panel report," and further that "subsequent panels did not feel bound by the details and reasoning of a panel report",

⁵⁹*Ibid.*, at 23.

⁶⁰See, *ibid.*, *supra* note 21, para. 6.10.

⁶¹*Ibid.*

referring to the EEC Import of Dessert Apple case.⁶² Such a historical explanation is deemed to constitute sufficient grounds for arriving at the above conclusion.

iii) Purpose of Article III

The findings of the AB in this report seems to be reasonable. According to the AB, the protection of negotiated tariff concessions under Article II is certainly one purpose of Article III. Nonetheless, this should not be overemphasised because the scope of Article III was not limited to products that were the subject of tariff concessions under Article II.⁶³

a) "*like products*"

This case explained an important criteria with regard to the term "like products". In the Panel Report, the meaning of the term "like product" in Article III:2 was treated differently from that in Article III:4, namely, the former referred to like product and directly competitive or substitutable product, while the latter mentioned only like product. According to the Panel Report, the term "like product" should be construed narrowly in the case of Article III:2, first sentence.⁶⁴ The AB agreed with the Panel on this point.

However, the AB disagreed with the Panel's observation (in para. 6.22) that the distinction between "like product" and "directly competitive or substitutable products" under Article III:2 was "an arbitrary decision". The AB amended this wording to "a discretionary decision" that must be made by considering the various characteristics of products in individual cases.

The AB upheld the Panel's reasoning on the decisive criterion to be used in determining whether products were "like" or "directly competitive or substitutable". As for deciding "likeness" of products, they must have not only common end uses but also common physical characteristics; while, with respect to "direct competitiveness or substitutability" of products, they must have common end-uses

⁶²The Panel Report on EEC - Restrictions on Imports of Dessert Apples (EEC - Desert Apples), adopted on 22 February 1959, BISD 36S/93 at para. 12.1.

⁶³The Report of the AB on Japan - Alcohol-II, *supra* note 53, Section G.

⁶⁴The Report on Japan - Alcohol-I, *supra* note 21, para. 6.20, which was reproduced in the Report of the AB, *ibid.*, Footnote 55.

which may be shown by elasticity of substitution.⁶⁵

b) *determination of the likeness of products*

The Panel examined the following tests, the so-called "two-step" test and the "aim-and-effect" test. The Panel rejected the aim-and-effect test because of the following reasons: (i) the difficulty of demonstrating the purpose of legislation; (ii) the potential misuse of the burden of proof, for example, this test could seek for exceptions under Article XX (General Exceptions). To reject the aim-and-effect test proposed by the U.S. and Japan, the Panel had to reject previous cases in which this test was employed. Those cases were: the U.S. - Auto Taxes (unadopted) and the U.S. - Malt Beverages (adopted). It seems that the Panel in this case tried to clarify the validity of the aim-and-effect test for its analysis of Article III:2.

c) *"In excess of"*

The AB agreed with the Panel's legal reasoning and its conclusion on this aspect. Namely, if the products were found as "like products", even the smallest amount of "excess" was deemed to be illegal.⁶⁶ In other words, the *de minimis* exemption was not available.

d) *"directly competitive or substitutable products"*

According to the AB, in the same way as for "like products", the determination of the appropriate range of "directly competitive or substitutable products" must be made on a case-by-case basis. It seemed appropriate to look at competition in the relevant markets as one of the means available to identify the broader category of products that might be described as "directly competitive or substitutable". AB supported the Panel whereby that the elasticity of substitution in the relevant market should be examined to determine whether products were "directly competitive or substitutable". Nonetheless, the AB noted that the Panel made an error of law by not addressing the test to the full range of alcoholic beverages included in the Terms of Reference.⁶⁷

⁶⁵The Report on Japan - Alcohol-I, *supra* note 21, para. 6.22.

⁶⁶U.S. - Malt Beverages, *supra* note 42, at para. 5.6; U.S.- Superfund, *supra* note 52 at para. 5.1.9.; Japan - Alcohol-II, *supra* note 21 at para. 5.8.

e) *"Not similarly taxed"*

The AB challenged the Panel's reasoning in arriving at its decision that "if directly competitive or substitutable products were 'not similarly taxed', and if it were found that the tax favoured domestic products, then protection would be afforded to such products, and Article III:2, second sentence, would be violated".⁶⁸ However, in the view of the AB, the standard of "not similarly taxed" and that of "so as to afford protection" were different. Nonetheless, the AB agreed with the Panel that the amount of difference in taxation had to be more than *de minimis* to be deemed "not similarly taxed".⁶⁹ In addition, the AB supported the Panel's reasoning that whether any particular differential amount of taxation was *de minimis* or not had to be determined on a case-by-case basis. In short, to be "not similarly taxed", the tax burden on imported products must be heavier than on "directly competitive or substitutable" domestic products, and furthermore that burden must be more than *de minimis*.

f) *"so as to afford protection to domestic production"*

The Panel equated dissimilar taxation above a *de minimis* level with the "separate and distinct" (as the AB held above) requirement of demonstrating that the tax measure "affords protection to domestic production". According to the report of the AB, the dissimilar taxation must be more than *de minimis*. Furthermore, the dissimilar taxation levied differently must also be applied "so as to afford protection" to domestic products. In addition, a determination of "the existence of protective taxation" must be made based on a careful, objective analysis of each and all relevant facts and all the relevant circumstances.

vi) A new approach to interpretation could be recognised in the reports of Panel and AB

⁶⁷See the Report on Japan - Alcohol-II, *supra* note 21, para. 7.1(ii) which referred only to "shochu, whisky, brandy, rum, gin, genever, and liqueurs". The U.S., in fact, referred the range of products to the DSB as "all other distilled spirits and liqueurs falling within HS heading 2208" (see WT/DS11/2).

⁶⁸The Report on Japan - Alcohol-II, *ibid.*, para. 6.33.

⁶⁹*Ibid.*

The reports of Panel and AB extensively dealt with treaty interpretations.⁷⁰ The customary law rules for textual, systematic and functional methods of treaty interpretation⁷¹ were becoming more evident in panel practice. In addition, Article 3:2 DSU explicitly refers to it: "The Members recognise that the WTO DS mechanism serves to preserve the rights and obligations of Members under the covered agreements, and to clarify the existing provisions of those agreements *in accordance with customary rules of interpretation of public international law*" (emphasis added). The customary rules of interpretation of public international law are codified by Articles 31 and 32 of the VCLT, which is often cited to when interpreting a treaty, such as, the WTO Agreement.⁷² However, this legal concept had not explicitly been referred to previously (which was rather unpopular during the GATT period) and, in fact, most disputes were resolved within the scope of GATT jurisdiction.⁷³ Accordingly, the GATT Panel often had recourse to the drafting history of GATT (or the drafting history of the Havana Charter) which should have been referred to only as a "supplementary means of interpretation" under public international law, *inter alia*, under Article 32 of the VCLT.⁷⁴ In this respect, the

⁷⁰See, *ibid.*, Section D. "Treaty Interpretation".

⁷¹Petersmann, E.-U., The GATT/WTO Dispute Settlement System: International Law, International Organisations and Dispute Settlement [hereinafter, the "GATT/WTO DS System"], Kluwer Law International Ltd., the Hague, 1997 at 113.

⁷²See, *Territorial Dispute (Libyan Arab Jamahiriya/Chad)*, ICJ Reports 1994, p.6, at p. 21, para. 41, reaffirmed in *Maritime Delimitation and Territorial Questions Between Qatar and Bahrain (Jurisdiction and Admissibility)*, ICJ Reports 1995, p.6, at p.21, para. 33 (see also cases cited in Sinclair, Ian., The Vienna Convention on the Law of Treaties, 2nd ed., Manchester University Press, Manchester, 1984, Chapter Five, pp. 114-158). This view is also reflected in the WTO practice: apart from the present case (Japan - Alcohol-I, **BISD 34S/83**), see for example: the Panel Report on "EC - Cotton Yarn", **ADP/137** (30 October 1955), paras. 540ff; the Panel Report on "US - Reformulated Gasoline", **WT/DS2/R** (29 January 1996), **WT/DS2/AB/R** (29 April 1996) at 16 and also *ILM* 1996, pp. 247-300, 603-634; the AB Report on "Japan - Alcohol-II", *supra* note 53 (1 November 1996); the Report of the Panel and the AB on "US - Cotton Underwear", **WT/DS24/R**, **WT/DS24/AB/R** (25 February 1997); the Report of the Panel and the AB on "Brazil - Desiccated Coconut", **WT/DS22/R**, **WT/DS22/AB/R** (20 March 1997) (this case referred to the VCLT extensively); the Report of the Panel and the AB on "EC - Bananas", **WT/DS27/R/ECU**, **WT/DS27/R/GTM**, **WT/DS27/R/MEX**, **WT/DS27/R/USA**, **WT/DS27/AB/R** (25 September 1997); the Panel Report on "EC - Hormones", **WT/DS6/R/USA**, **WT/DS6/R/CAN** (24 September 1997).

⁷³According to Professor Petersmann, "*Under the GATT 1947, most panel reports have not devoted much space to explaining their methods of treaty interpretation*"., in E.-U. Petersmann, The GATT/WTO DS System, *supra* note 71 at 112.

⁷⁴"Up to the 1980's panels often attached undue importance to the drafting history of GATT 1947 which, should be used only as a supplementary means of interpretation in view of the

Panel and AB seem to have made efforts to clarify treaty interpretation in accordance with customary rules as defined in the VCLT.

Second, the Panel demonstrated its "strict" rule-oriented attitude in light of the issues in dispute throughout the DS procedures (e.g., para. 6.26 of the Panel report) which eventually resulted in favouring the EC's arguments. Nonetheless, despite the request by Japan, the Panel did leave aside the issue of the legality of the Alcohol Tax System of the Complainants. In other words, the Complainants must have been aware of some impact on their Alcohol Tax System in future cases. In this regard, the present case will have substantially influenced future cases dealing with similar issues originating from the Complainants' tax system.

Third, the Panel used the issue of "tariff" (or customs duties) as one of the grounds for issuing recommendations which decided that Japan's Liquor Tax Law was not in accordance with the GATT rules. Nonetheless, a tariff is one of the border controls or measures used in order for a country to protect its national industries in accordance with tariffs agreed under the GATT/WTO rule. In other words, a tariff is the only means of protection permitted under the GATT/WTO system. Furthermore, one should recall that a principal goal of the GATT is to promote trade liberalisation through substantial reduction of tariffs (through tariff negotiations conducted in accordance with the GATT rule provided in Article XXVIII bis), which can be found in the Preamble to the General Agreement. The Preamble states: "Being desirous of contributing to these objectives by entering into reciprocal and mutually advantageous arrangements *directed to the substantial reduction of tariffs* and other barriers to trade and to the elimination of discriminatory treatment in international commerce" (emphasis added).⁷⁵ This paragraph was once again reiterated in the Preamble to the WTO Agreement. Accordingly, one could recognise the proper goal of tariffs (i.e. protection of national products in accordance with certain conditions such as agreed tariff concessions) as being clearly indicated in the text. In the present

fact that, for example, most GATT contracting parties did not participate in the drafting of the GATT 1947", ibid., at pp. 112-113.

⁷⁵See, the Preamble of the General Agreement on Tariffs and Trade (GATT).

case, however, the issue was whether Japan's national legislation (i.e. internal measures such as taxation and regulation) was in violation of Article III. It, therefore, excluded the issue of border controls/measures (i.e. tariffs/customs duties), from the scope of this provision. For this reason, it seems fair to say that the Panel examined an issue beyond its original terms of reference which were merely concerned with the legality of Japan's national measures under Article III.

v) Japan's tactical approach in DS proceedings

It should be noted that Japan made a timely response to the U.S. over the issue of terms of reference. Although the U.S. requested consultations with Japan under GATT Article XXII concerning internal tax imposed by Japan on certain alcoholic beverages pursuant to the Liquor Tax Law (WT/DS11/1), the U.S. later tried to expand the factual and legal basis of its original claim,⁷⁶ which stated "*...the reduction in excise taxes for small volume producers, contained in the 1989 legislation, discriminates on its face against imported shochu, sake and wine and therefore violates Article III:2 first sentence*". Japan responded to this U.S. claim immediately and condemned the U.S. for its action. Furthermore, Japan promptly requested the Panel to consider that the U.S. claim as being beyond the terms of reference of the present case.⁷⁷ The Panel turned down the U.S. claim regarding the Japanese Taxation Special Measures Law, and only dealt with the other claims.⁷⁸ In this respect, unlike its previous behaviour in such matters, Japan responded efficiently and promptly to this U.S. tactic and eventually succeeded in overcoming it.

⁷⁶Cf. Japan - Measures Affecting Distribution Services, complained by the U.S. (WT/DS45) on 13 June 1996. Later, on 20 September 1996, the U.S. requested further consultations with Japan in order to stretch or expand its original claim in terms of the factual and legal basis.

⁷⁷The Report on Japan - Alcohol-I, *supra* note 21, para. 4. 3.

⁷⁸See, *ibid.* para. 6.5. which stated that "...concluded that its terms of reference do not permit it to entertain the claim of the United States with respect to the Japanese Taxation Special Measures Law and it proceeded, therefore, to examine the other claims".

vi) Careless statements in Japan's argument

Although Japan displayed sound tactics during the panel proceedings, it also made careless statements in its argument. For instance, with respect to the interpretation of Article III:2, second sentence, Japan argued: "the 'effect' of 'so as to afford protection' must be judged by whether the tax distorts the competitive relationship between imported and domestic products" (para. 4.153). Japan argued that the Liquor Tax Law did not distort the competitive relation between imported and domestic products because "the tax/price ratios of all tax categories are *roughly the same*. Concerning the examination of the tax burden, the tax/price ratio is a superior yardstick and better indicates the impact on consumers' choice than the ratio of tax over product volume or alcohol content...(emphasis added); ..." (para. 4.153). To support this argument, Japan submitted charts (one is on the Average Retail Prices and Taxes of Liquor, and the other on the Percentage of Taxes in Retail Prices) which identified the "roughly the same" tax/price ratios in Annex VI of the Panel Report (para. 4.143). Nonetheless, among the evidence rebutted by the Community, it was pointed out that "[t]he tax/price ratio calculated by Japan is *far from being 'roughly constant'* (emphasis added) (para. 6.155).

Following the arguments put by the parties to the dispute, the Panel addressed the argument submitted by Japan which, in the Panel's view, aimed to achieve horizontal equity (i.e. a level playing field, namely, requires the same tax burden regardless of a various level of tax-bearing ability).⁷⁹ Nonetheless, since the aim-and-effect test put forward by Japan and the U.S. had already been dismissed by the Panel, the Panel noted that Japan's argument could be regarded as being that Liquor Tax Law taxed directly competitive or substitutable products similarly. The Panel considered that this argument should be rejected due to the following reasons (para. 6.34):

- a) The benchmark in Article III:2, second sentence, is whether internal taxes operate "so as to afford protection to domestic production", which means dissimilar taxation of domestic and foreign directly competitive or substitutable products; ... the Panel considered that *it is not at all clear that maintaining a "roughly constant" tax/price ratio avoids violating this requirement* (emphasis added);

⁷⁹See, *ibid.*, para. 4.132ff.

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b) The statistics on the tax/price ratio indicate that *significant differences exist* between shochu and the other directly competitive or substitutable products and also that there are *significantly different tax/price ratios* within the same product categories. Therefore, the tax/price ratios *could not be regarded as being "roughly constant"*, and horizontal equity could not be demonstrated;

... there were significant problems with the methodology used for calculating tax/price ratios submitted by Japan (para. 6.33), thus arguments based on that methodology could be regarded as inconclusive;

... its statistics on which the tax/price ratios were based excluded domestically produced spirits and whisky/brandy from the calculation of tax/price ratios for spirits and whisky/brandy. Since the prices of the domestic spirits and whisky/brandy are much lower than the prices of the imported ones, this exclusion has the impact of reducing considerably the tax/price ratios cited by Japan for those products.

In this connection, ...one consequence of the Japanese tax system was to make it more difficult for cheaper imported brands of spirits and whisky/brandy to enter the Japanese market (emphasis added); and,

c) ... the purpose of [the contested legislation], i.e. maintaining a constant tax/price ratio was not mentioned in the legislation. This is *ex post facto* rationalisation by Japan, and ... there are *no guarantees in the legislation that the tax/price ratio will always be maintained at a constant (or "roughly constant") level* (emphasis added).

Consequently, the Panel considered that Japan's argument should be rejected. As examined above, first of all, it seems that the phrase, "roughly constant", was not persuasive in the Panel's view. In this regard, Japan argued that the tax/price ratios under the legislation calculated by Japan was neutral, and furthermore Japan submitted the data which was supposed to demonstrate the neutrality of the tax. On the contrary, the data was deemed as evidence which showed it not to be neutral. The percentage of taxes on retail prices might vary from 5 to 22 percent, which seemed quite different from what Japan had argued. Therefore, there was some weakness in Japan's argument which was consequently unconvincing. It seems that Japan made careless statements in its arguments which led Japan to being in an disadvantageous position and eventually gave a negative impression to the Panel. To sum up, the Japanese argument seemed to be based on a *de facto* rationalisation of its Liquor Tax Law. Accordingly, this point was not appreciated from a legal point of view by the Panel.

vii) Others

It should be mentioned that one phenomenon, subsequent to the present panel has become apparent, that is, the WTO ruling against Japan has already triggered similar cases against other member states (i.e., South Korea and Chile respectively) as had been anticipated. First, complaints against Korean taxes on alcoholic beverages were made by the EC (WT/DS/75/1) on 4 April 1997 and the U.S. (WT/DS84/1) on 23 May 1997.⁸⁰ Chilean taxes on alcoholic beverages were complained against by the EC (WT/DS87/1) on 4 June 1997.⁸¹ Furthermore, one can expect a number of similar cases to be brought in the future. Since the WTO Panel has already expressed its opinion over similar issues in the present Japanese case, it will be worth examining those forthcoming reports for the purpose of comparison, but I leave this for a future project.

⁸⁰On 13 July 1998, the Panel issued a panel report which supported the U.S. (complainant) challenge to Korean laws, see "WTO Panel Backs U.S.-EU Case by Shooting Down Korean Liquor Tax", Inside US Trade, 7 August 1998; Report of the Panel on Korea - Taxes on Alcoholic Beverage, WT/DS75/R; WT/DS84/R (17 September 1998); On 20 October 1998, Korea appealed certain issues of law covered in the Panel Report and legal interpretations developed by the Panel. The appellate body informed that it would not be able to circulate its Report by 21 December 1998 due to the time required for translation of the Report (according to Article 17.5 of the DSU, the Appellate Body will circulate its report no later than 60 days after the appellant has formally notified its decision to appeal; in this case, the 60-day period would expire on Monday, 21 December 1998). Instead, the Report of the Appellate Body was circulated to WTO Members by Monday, 18 January 1999; see Korea - Taxes on Alcoholic Beverages: Communication from the Appellate Body, WT/DS75/10, WT/DS84/8 (17 December 1998); for the report of the Appellate Body, WT/DS75/AB/R; WT/DS84/AB/R (18 January 1999).

⁸¹This request is in respect of Chile's Special Sales Tax on spirits, which allegedly imposes a higher tax on imported spirits than on "Pisco" (a locally brewed spirit). The EC contends that this differential treatment of imported spirits violates Article III:2 of GATT 1994. The panel was established on 18 November 1997. In addition, on 15 December 1997, the EC made another request in respect of Chile's internal tax regime for alcoholic beverages complained of by the EC (DS87) and by the U.S. (DS109). The EC's request concerns with the modification to the law on taxation on alcoholic beverages passed by Chile to address the concerns of the EC (DS87). The EC contends that the modified law still violates GATT Article III:2. The DSB established a panel on 25 March 1998. The DSB agreed, pursuant to Article 9.1 of the DSU, that the two complaints be examined by a single panel; the Chairman of the Panel circulated communication regarding delay of its work. According to the communication, it will be impossible for this Panel to complete its work in six month "due to the parties' wish to use the maximum time periods prescribed in Appendix 3 of the DSU". The Panel now expects to circulate the final report to the parties by the end of April 1999; see for Communication from the Chairman of the Panel, WT/DS87/7; WT/DS110/6 (25 January 1999); Report of the Panel on Chile - Taxes on Alcoholic Beverage, WT/DS87/R; WT/DS110/R (circulated to the Members on 26 March 1999).

8.1.2.2. The Film Case⁸²**Background:**

The present case was initiated with the Kodak's petition (18 May 1995) under Section 301 of the Trade Act of 1974 with the USTR. On 3 July 1995, the USTR commenced an investigation and subsequently requested bilateral consultations with Japan. The MITI, however, refused this U.S. request.⁸³ On 13 June 1996, the U.S. finally requested consultations with Japan regarding certain Japanese "unreasonable"⁸⁴ tolerance of anticompetitive practices in the film market.⁸⁵ On 20 September 1996, the U.S. requested the establishment of a Panel⁸⁶ and in its request the U.S. made certain allegation concerning Japan's implementation and maintenance of certain laws, regulations, requirements and measures (or "*taisaku*" in Japanese)⁸⁷ affecting the distribution, offering for sale, and internal sale of imported consumer photographic film and paper.

Summary of Arguments:

The gist of the claims raised by the U.S. was that 21 Japanese measures,⁸⁸ though not in violation of WTO rules, impaired the "legitimate expectations" of the U.S. (by

⁸²Report of Panel on Japan - Measures Affecting Consumer Photographic Film and Paper (Japan - Film), WT/DS44/R (31 March 1998).

⁸³See, Letter from MITI Vice-Minister Yoshihiro Sakamoto to USTR Ambassador Ira Shapiro, reproduced in Inside US Trade, 12 January 1996 at 23-24.

⁸⁴For the definition of "unreasonable", see Trade and Tariff Act of 1984, Pub. L. No. 98-573, 98 Stat. 2948, 19 U.S.C. §2411(d)(3)(A), (B) (1984).

⁸⁵WT/DS44/1 (21 June 1996).

⁸⁶On 12 December 1996, the U.S. requested the DG to determine the composition of the Panel (Article 8.7 DSU); On 17 December 1996, the DG composed of the Panel consisting of Mr. William Rossier (Switzerland) as Chairman, Mr. Adrian Macey (New Zealand) and Mr. Victor Luis do Prado (Brazil) as panellists; the Panel held two substantive meetings with the parties to the dispute: the first was held on 17 and 18 April 1997, and the second on 2 and 3 June 1997 (the Panel had one meeting with the third parties to the dispute, i.e. the EU and Mexico, on 18 April 1997).

⁸⁷The parties raised translation problems (in total, 24 separate translation issues) including the term "*taisaku*". "*Taisaku*", for example, was translated as (liberalisation) "countermeasures" by the U.S. or as (liberalisation) "measures" by Japan. For resolving this issue, the Panel, accordingly, pursuant to Article 13 of the DSU, appointed two Japanese language experts, i.e. Professor Zentaro Kitagawa (Kyoto Comparative Law Centre, Japan) and Professor Michael Young (Columbia University, New York) [para. 1.10 of the Panel Report in WT/DS44/R (31 March 1998)]; for the Procedure for the Resolution of Possible Translation Issue, see, *ibid.* para. 1.9.; The reports by these experts are attached as an "Annex on Translation Problems" in Section XI of the Panel Report.

⁸⁸The List of 21 Measures at Issue:

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virtue of the tariff negotiations of the Kennedy, Tokyo and Uruguay Rounds) for access to the Japanese photographic film market. The U.S., in this case, grouped 21

1. DISTRIBUTION MEASURES

- (1) 1967 Cabinet Decision
- (2)*Japan Fair Trade Commission Notification 17 on Premiums to Business (1967 JFTC Notification 17)
- (3)*1968 Sixth Interim Report on "Distribution Modernisation Outlook and Issues" (1968 Sixth Interim Report)
- (4) 1969 Seventh Interim Report on "Systemisation of Distribution Activities" (1969 Seventh Interim Report)
- (5) 1969 Survey on Transaction Terms (1969 Survey)
- (6) 1970 Guidelines for Rationalising Terms of Trade for Photographic Film (1970 Guidelines)
- (7)**1971 International Contract Notification under the Antimonopoly Law and JFTC Rule 1 (1971 International Contract Notification requirement)
- (8) 1971 Basic Plan for Systemisation of Distribution (1971 Basic Plan)
- (9) 1975 Manual for Systemisation of Distribution by Industry: Camera and Film (1975 Manual)
- (10)**1976 Japan Development Bank funding to Konica for joint distribution facilities (1976 JDB funding for Konica's wholesalers)
- (11)**1977 Small and Medium Enterprise Agency financing to photoprocessing laboratories (1977 SMEA funding for photoprocessing laboratories)

2. RESTRICTIONS ON LARGE RETAIL STORES

- (12) 1974 Large Scale Retail Stores Law (1974 Large Stores Law)
- (13) 1979 Diet amendment to Large Stores Law (1979 Amendment)

3. PROMOTION MEASURES

- (14)**1971 JFTC Notification 34 on open lotteries (1971 JFTC Notification 34)
- (15)*1977 JFTC Notification 5 on Premiums to Consumers (1977 JFTC Notification 5)
- (16) 1981 JFTC Guidance on Dispatched Employees
- (17) 1982 Self-Regulating Rules Concerning Fairness in Trade with Business (1982 Self-Regulating Rules)
- (18) 1982 Establishment of Fair Trade Promotion Council (1982 Promotion Council)
- (19)**1983 JFTC guidance on the establishment of rules on loss-leader advertising and dumping (1983 JFTC guidance on advertising rules)
- (20) 1984 Self-Regulating Standards Concerning Display of Processing Fees for Colour Negative Film (1984 Self-Regulating Standards)
- (21) JFTC approval of the 1987 Retailers Code and its enforcement body, the Retailers Fair Trade Council (1987 Retail Code)

Note 1: Japan argued that those measures marked with an asterisk(s) were not properly before the panel because of procedural defects in the U.S. complaint (para. 3.11).*

*Under the heading "Procedural Objections" (Section III, B of the Panel Report), Japan requested the panel to dismiss some of the US claims because these "measures" were raised by the U.S. for the first time in its initial submission to the Panel, and had not been identified specifically in the request for the establishment of the panel. Article 6:2 DSU requires the complaining party "to identify the *specific measures at issue*" (emphasis added). In Japan's view, the U.S. requests for consultations as well as the establishment of a panel insufficiently identified the measures in dispute, and particularly the U.S. panel request did not fulfil the specificity requirements prescribed in Article 6:2 DSU; Japan also argued that the U.S. request for consultations was "overly broad and vague", and did not identify the measures as required in Article 4:4 DSU which read: "Any request for consultations shall be submitted in writing and shall give reasons for the request, including *identification of the measures at issue* and an *identification of the legal basis* for the complaint" (emphasis added).

Note 2: The Panel sustained Japan's procedural objections (*Note 1*) in respect of 5 measures, marked with two asterisks above, which were not within the Panel's terms of reference.

measures into 3 broad categories: (i) *distribution measures*, which allegedly encouraged and facilitated the creation of a vertically integrated market structure for photographic film and paper in which imports were excluded from traditional distribution channels; (ii) *restrictions on large stores* (i.e. Large Stores Law), which allegedly restricted the growth of alternative distribution channels for imported film; and (iii) *promotion measures*, which allegedly disadvantaged imports by restricting the use of sales promotion techniques.

In this case, the U.S. alleged the following:

- "The distribution countermeasures, Large Stores Law and related measures, and promotion countermeasures in combination nullify or impair benefits within the meaning of Article XXIII:1(b);

- "The distribution countermeasures, as a set, also

i. violate Article III:4 and

ii. nullify or impair benefits within the meaning of Article XXIII:1(b);

- "The Large Stores Law and related measures also nullify or impair benefits within the meaning of Article XXIII:1(b), in the context of the restrictive distribution structure in Japan;

- "The promotions countermeasures, as a set, nullify or impair benefits within the meaning of Article XXIII:1(b), in the context of the restrictive distribution structure in Japan;

- "The specific failures to publish the fair trade councils' and JFTC enforcement actions as well as guidance by MITI, prefectural and local authorities under the Large Stores Law or related local regulations, that establish or modify criteria applicable in future cases, each constitute a violation of Article X:1." (para. 4.26)

Japan rejected all these U.S. claims. In Japan's view, "none of the alleged measures individually adversely affected imported products or altered the conditions of competition facing imported products; Japan further emphasised that even if these three broad categories of measures were considered as 'sets of measures' with combined effects, they did not in any way disadvantage imports because combining nothing with nothing still produces nothing".⁸⁹

⁸⁹The Report on Japan - Film, *supra* note 82, para. 4.27.

Summary of Findings and Conclusions:

1. Procedural objection

Of 21 Japanese measures objected to by the U.S., Japan argued that 8 measures were outside the Panel's terms of reference and were not proper to be put before the Panel because of procedural defects in the complaint. The Panel sustained Japan's procedural objections with respect to 5 measures⁹⁰ out of 8 because the U.S. had not complied with the requirements of Article 6:2 DSU which requires the complaining party to "identify the specific measures at issue" when requesting the establishment of a panel. Furthermore, these items had not been mentioned in the U.S. panel request, nor were they subsidiary or closely related to measures specifically identified. In addition, the Panel decided that the 3 remaining measures⁹¹ out of 8 were within its terms of reference because they were also subsidiary or closely related to measures specifically identified (i.e. the respondent and third parties had received adequate notice of the scope of the complainant's claims). (paras. 10.20-10.21)

2. Non-violation claims

As mentioned earlier, the U.S. grouped measures of the Japanese government into 3 categories, namely, distribution measures; restrictions on large retail stores; and promotion measures. The central theme of the U.S. claim was that these three sets of measures attributable to the Government of Japan, though not in violation of WTO rules, impaired or nullified, individually and in combination, the legitimate expectations of U.S. (which, in the U.S. view, resulted from the tariff concessions granted by Japan in the Kennedy, Tokyo and Uruguay Rounds of tariff negotiations) for access to the Japanese photographic film market.

With respect to the non-violation claim under the GATT, Article XXIII:1(b) reads:

⁹⁰(i) 1976 JDB funding to Konica for joint distribution facilities; (ii) 1977 SMEA funding photoprocessing laboratories; (iii) 1971 International Contract Notification requirement (and Rule 1 under Article 6 of the Antimonopoly Law); (iv) 1971 JFTC Notification 34; and (v) 1983 JFC guidance on advertising and dumping.

⁹¹(i) 1968 Sixth Interim Report; (ii) 1967 JFTC Notification 17; and (iii) 1977 JFTC Notification 5.

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"If any Member should consider that any *benefit* accruing to it directly or indirectly under this Agreement is being *nullified or impaired* ... as the result of ... (b) the *application* by another Member of any *measure, whether or not it conflicts* with the provisions of this Agreement ... " (emphasis added).

Despite its recognition under the GATT/WTO rules, there have only been three successful non-violation cases (out of, just eight cases in which panels or working parties have substantively considered Article XXIII:1(b) claims⁹²) brought in the fifty-years-history of GATT. In the most recent successful case, the Oilseeds panel, a persuasive explanation for the purpose of Article XXIII:1(b) was expressed:

"The idea underlying [the provisions of Article XXIII:1(b)] is that the improved competitive opportunities that can legitimately be expected from a tariff concession can be frustrated not only by measures prescribed by the General Agreement but also by measures consistent with that Agreement. In order to encourage contracting parties to make tariff concessions they must therefore be given a right of redress when a reciprocal concession is impaired by another contracting party as a result of the application of any measure, whether or not it conflicts with the General Agreement".⁹³

...

"The Panel considered that the main value of a tariff concession is that it provides an assurance of better market access through improved price competition. Contracting parties negotiate tariff concessions primarily to obtain that advantage. They must therefore be assumed to base their tariff negotiations on the expectation that the price effect of the tariff concessions will not be systematically offset. If no right of redress were given to them in such a case they would be reluctant to make tariff concessions and the General Agreement would no longer be useful as a legal framework for incorporating the results of trade negotiations".⁹⁴

⁹²*Report of the Working Party on Australian Subsidy on Ammonium Sulphate, adopted on 3 April 1950, BISD II/188; *Panel Report on Treatment by Germany of Imports of Sardines ("Germany - Sardines"), G/26, adopted on 31 October 1952 BISD 1S/53; Uruguayan Recourse, adopted on 16 November 1962, BISD 11S/95; Panel Report on EC - Tariff Treatment on Imports of Citrus Products from Certain Countries in the Mediterranean Region ("EC - Citrus Products"), L/5576 [7 February 1985 (unadopted)]; Panel Report on EEC - Production Aids Granted on Canned Peaches, Canned Pears, Canned Fruit Cocktail and Dried Grapes ("EEC - Canned Fruits"), L/5778 [20 February 1985 (unadopted)]; Japan - Semi-conductors, adopted on 4 May 1988, BISD 35S/116; *EEC - Oilseeds, adopted on 25 January 1990, BISD 37S/86; United States - Agricultural Waiver, adopted on 7 November 1990, BISD 37S/228 (those cases marked with an asterisk are three successful ones).

⁹³EEC - Oilseeds, *ibid.*, 126-127, para. 144.

⁹⁴*Ibid.*, para. 148.

Both GATT contracting parties and WTO Members have treated a non-violation claim with caution and have treated it as *an exceptional remedy* which requires the complaining party to provide a detailed justification to support its allegations. Article 26:1 DSU confirms this point as follows:

"Where and to the extent that such party considers and a panel or the Appellate Body determines that a case concerns a measure that does not conflict with the provisions of a covered agreement to which the provisions of paragraph 1(b) of Article XXIII of GATT 1994 are applicable, the procedures in this Understanding shall apply, subject to the following:

(a) *the complaining party shall present a detailed justification* in support of any complaint relating to a measure which does not conflict with the relevant covered agreement ...".⁹⁵ (emphasis added)

As explained, the requirements for establishing a non-violation case are stricter than those in a violation case. A "detailed justification" with respect to three elements are required to be demonstrated:

- i) that a governmental measure exists;
- ii) that it was not anticipated at the time of the relevant tariff negotiations; and
- iii) that it upsets the competitive relationship between imported and domestic products.

i) Governmental measures

To begin with, the present dispute centred on whether the "measures" cited were governmental and whether they were still in effect. Japan argued that several of the measures cited were merely studies by non-governmental bodies or actions taken by private organisations. The U.S. countered, however, that such Japanese studies (by order of the MITI) or actions taken by private organisations were equivalent to governmental action. Those issues have been considered in three GATT cases dealt with below, involving Japanese government "administrative guidance" and a Japanese-government approved "fair competition code" applicable to a private association. The definitions of "measures" of each party are:

⁹⁵Article 26:1 DSU was reproduced in para. 10.30 of the Reports on Japan - Film, *supra* note 82.

In the Japanese view, it must provide benefits or impose obligations. In other words, it must be a governmental policy or action which imposes legally binding obligations or their substantive equivalent. While, in the U.S. view, it should not be limited to refer only to legally binding obligations or their substantive equivalent and should be given a broader definition.

a) "*administrative guidance*"

The issue of government attributability had been considered in the following GATT cases which involved "administrative guidance" of the Japanese government and a Japanese-government approved "fair competition code" applicable to a private association.

1. In the Japan - Semiconductor case, the Panel held that where administrative guidance *creates incentives or disincentives largely dependent upon governmental action for private parties to act in a particular manner*, non-mandatory measures would be operating in a manner equivalent to mandatory requirements so that *the difference was only one of form and not of substance*.⁹⁶ (emphasis added) (para. 10.54)
2. In the Japan - Agricultural Products case, informal administrative guidance to restrict production of certain agricultural products could be considered to be a governmental measure because it was a traditional tool of Japanese Government policy *based on consensus and peer pressure*, and due to *its effectiveness in the Japanese context* in spite of its lack of transparency.⁹⁷ (emphasis added)
3. In the EEC - Dessert Apples case, the Panel noted that the EEC internal regime for apples was *a hybrid one, which combined elements of public and private responsibility*, namely, direct buying-in of apples by Member State authorities and

⁹⁶Japan - Semiconductors, BISD 35S/116 at 155; see Section 7.1.1.4. of this thesis.

⁹⁷Panel Report on Japan - Restrictions on Imports of Certain Agricultural Products ("Japan - Agricultural Products"), adopted on 22 March 1988, BISD 35S/163, 242; Section 7.1.1.3. of this thesis.

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withdrawals by producer groups, and considered both systems to be governmental measures.⁹⁸ (emphasis added) (para. 10.55)

In the Panel's view, a government policy or action need not necessarily have a substantially binding or compulsory nature for it to entail a likelihood of compliance by private actors in a way so as to nullify or impair legitimately expected benefits within the purview of Article XXIII:1(b). Furthermore, in cases where *there was a high degree of co-operation and collaboration between government and business* (e.g. where there was substantial reliance on "administrative guidance" and other more informal forms of a government-business co-operation), it was conceivable that even non-binding, hortatory wording in a government statement of policy could have a similar effect on private actors as legally binding measure or what Japan referred to as regulatory "administrative guidance". (para. 10.49)

The Panel, furthermore, stated that the incentive/disincentive test (in the Japan - Semiconductors panel) should not be deemed as an exclusive means of characterising formally non-binding measures as governmental.⁹⁹ The Panel on EEC - Parts and Components considered that the term "*laws, regulations or requirements*" included requirements which an enterprise voluntarily accepts in order to obtain an advantage from the government.¹⁰⁰ Given that the scope of the word *requirement* would seem to be narrower than that of *measure*, the broad reading given to the word *requirement* by past panels supported an even broader reading of the word *measure*.¹⁰¹ The Panel, therefore, concluded that the term "measures" should be defined not in an unduly restrictive manner but on a *case-by-case basis*. Otherwise, there was a risk that cases, in which governments had been involved one way or another in the nullification or impairment of benefits (i.e. legitimate expectations of benefits arising

⁹⁸Panel Report on EEC - Dessert Apples (Complained by Chile), BISD 36S/93, 126, *supra* note 62.

⁹⁹*Ibid.*, para. 10.48.

¹⁰⁰Panel Report on EEC - Regulation on Imports of Parts and Components ("EEC - Parts and Components"), adopted on 16 May 1990, BISD 37S/132, 197, para. 5.21; see for the case study at Section 7.1.2.2. of this thesis.

¹⁰¹The Report on Japan - Film, *supra* note 82, para. 10.51.

from tariff negotiations) would not be redressable under GATT Article XXIII:1(b), thereby preventing the achievement of the purpose of non-violation claims.

b) *Continuing application and effect*

The Panel noted that the disputing parties agreed on the fundamental point that only a measure that continues to be applied, and not the market structure which may or may not result from the application of such measure, may be the basis for a cognisable non-violation complaint under GATT Article XXIII:1(b). Whereas, with respect to the issue whether or not certain of the "measures" in question were still in effect, the Panel noted the parties' disagreement. Japan argued that most of the "measures" ended years ago and thus were not currently actionable, while the U.S. contended that at most two "measures"¹⁰² were formally repealed and that all the policies underlying the "measures" continued currently in the form of "*continuing administrative guidance*". (para. 10.59)

Regarding the issue of the continuing effect of measures, it was not the practice of GATT/WTO panels to rule on measures which have expired or which have been repealed or withdrawn.¹⁰³ In only a very small number of cases, involving quite particular situations, had panels proceeded to adjudicate claims involving measures which no longer existed or which were no longer being applied.¹⁰⁴ (para. 10.58)

¹⁰²The two measures are: 1967 JFTC Notification 17; and 1971 International Contract Notification requirement.

¹⁰³See footnote 1221 of the Panel Report on Japan - Film, *supra* note 80, U.S. - Gasoline, WT/DS2/R, para. 6.19, where the Panel stated its opinion that "*it had not been the usual practice of a panel established under the General Agreement to rule on measures that, at the time the panel's terms of reference were fixed, were not and would not become effective*"; see further Panel Report on Argentina - Measures Affecting Imports of Footwear, Textiles, Apparel and Other Items (Argentina - Footwear), WT/DS33/R, circulated on 25 November 1997, pp. 84-86.

¹⁰⁴See footnote 1222 of the Panel Report on Japan Film, for example, Panel Report on U.S. - Wool Shirt and Blouses, WT/DS33/R, upheld by the AB, WT/DS33/AB/R, where the Panel ruled on a measure that was revoked after the interim review but before issuing the final report to the parties; Panel Report on EEC - Measures on Animal Feed Proteins (adopted on 14 March 1992), BISD 25S/49, where the panel ruled on a discontinued measure, but one that had terminated after the terms of reference of the Panel had already been agreed; Panel Report on United States - Prohibitions on Imports of Tuna and Tuna Products from Canada (adopted on 22 February 1982, BISD 29S/91, 106, para. 4.3., where the Panel ruled on the GATT consistency of a withdrawn measure but only in light of the two parties' agreement to this procedure; Panel Report on EEC - Restrictions on Imports of Apples from Chile

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The Panel did not rule out the possibility that old "measures" that were never officially revoked may continue to be applied through "*continuing administrative guidance*". Even if measures were officially revoked, the underlying policies may continue to be applied through "*continuing administrative guidance*". Nonetheless, the Panel noted that the burden was on the U.S. to demonstrate clearly that such guidance did in fact exist and that it was currently nullifying or impairing benefits. (para. 10.59)

Proceeding on its broad reading as to what constituted governmental attributability of measures in a Japanese context, the Panel found that 11 measures¹⁰⁵ were attributable to the Japanese government, 4 were non-governmental¹⁰⁶ and 1 originally governmental measure had been repealed.¹⁰⁷

Two reports, a survey and a manual authorised by private research institutes or MITI-affiliated councils were found to be non-governmental because of the merely descriptive and advisory nature of the studies. The Panel noted that they were general reports to the government and therefore could not be deemed as governmental exhortation to the private sector to take specific actions.

The Panel, however, assimilated to governmental measures: two sets of "self-regulating standards and rules" enacted by business associations in close consultation with governmental entities; two fair trade councils composed of private business on a voluntary basis which were created under the guidance of governmental entities, as well as fair competition codes that were enacted by such councils with the explicit authorisation of the JFTC. The Panel based these findings,

(adopted on 10 November 1980), **BISD 27S/98**, where the Panel ruled on a measure which terminated measure and, given its seasonal nature, there remained the prospect of its reintroduction.

¹⁰⁵These were: (i) 1967 Cabinet Decision; (ii) 1970 Guidelines; (iii) 1971 Basic Plan; (iv) 1974 Large Stores Law; (v) 1979 Amendment; (vi) 1977 JFTC Notification 5; (vii) 1981 JFTC Guidance on Dispatched Employees; (viii) 1982 Self-Regulating Rules; (ix) 1982 Promotion Council; (x) 1984 Self-Regulating Standards; and (xi) 1987 Retail Code.

¹⁰⁶These were: (i) 1968 Sixth Interim Report; (ii) 1969 Seventh Interim Report; (iii) 1969 Survey; and (iv) 1975 Manual.

¹⁰⁷1967 JFTC Notification 17.

inter alia, on the fact that compliance with JFTC-approved fair competition codes entailed involvement of the relevant council. Furthermore, the Panel did not reject the argument that the JFTC was likely to use these codes as a reference point for antitrust enforcement also against other companies that were active in the same sector of industry but which did not participate in the relevant council.

ii) The existence of reasonable anticipation

The U. S. claim was based on reasonable expectations of improved market access of foreign made photographic products accruing to tariff concessions made by Japan through three consecutive rounds of tariff negotiations, i.e. the Kennedy, Tokyo and Uruguay Rounds. Japan argued that the Uruguay Round was the only relevant round because it covered a new balance and assessment of tariff concessions.

In the Panel's view, two provisions of GATT 1994 appeared to be relevant for resolving this issue. Namely, the GATT 1994 (or the WTO legal system) incorporated protocols and certifications relating to tariff concessions under 1947 and the Marrakesh Protocol to GATT 1994. Furthermore, the Panel found, also in line with past GATT panel reports,¹⁰⁸ that reasonable expectations might co-exist with respect to tariff concessions made in successive rounds of Article XXVIII*bis* negotiations. (para. 10.64)

It is important to note that Japan made tariff concessions only on *black and white* photographic film and paper in the Kennedy Round. Thus, U.S. expectations from the Kennedy Round were limited to these items. Japan started making tariff concessions on colour film and paper at the Tokyo Round. (para. 10.71)

According to the U.S., it could not have anticipated the measures cited because, even at the time of the Uruguay Round, it could not fully appreciate the opaque nature of these Japanese measures. Japan submitted that most of the measures dated from the

¹⁰⁸See, EEC - Canned Fruit, L/5778 (unadopted); EEC - Oilseeds, *supra* note 92, BISD 37S/86.

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late 1960's and 1970's and must have been known to the U.S. and that, in any event, these measures did not change long-standing policies.

In the Panel's view, measures introduced and published subsequent to the conclusion of a tariff negotiation need not be presumed to be reasonably anticipated, whereas measures introduced prior to the conclusion of a tariff negotiation should be presumed. In this connection, in the Panel's view, (the U.S.) was charged with having knowledge of Japanese government measures as of the date of their publication. The Panel realised, however, that knowledge of the existence of a measure is not equivalent to understanding the impact of the measure on a specific product market. The Panel recognised the possibility of circumstances where the exporting country might not reasonably be aware of the significance of a measure for, or its potential impact on, imported products until some time after its publication. Nonetheless, the Panel expected the complaining party to clearly demonstrate why it could not have reasonably anticipated the effect of an existing measure on the film or paper market and when it did come to realise the effect. The Panel found that the simple statement by the U. S. that Japanese measures were so opaque and informal that their impact could not be assessed, was insufficient to show such exceptional circumstances. (para. 10.80)

With respect to the issue whether a measure was published prior or subsequent to the dates of the conclusion of the three rounds of tariff negotiations, the Panel found the following:

- The U.S. should have reasonably anticipated one particular measure¹⁰⁹ at the time of the Kennedy Round (1967);
- The U.S. should have anticipated all measures, except 5 of the promotion measures,¹¹⁰ at the time of the Tokyo Round (1979);
- The U.S. should have anticipated all measures at the time of the Uruguay Round (1993);

¹⁰⁹1967 JFTC Notification 17.

¹¹⁰1981 JFTC Guidance on Dispatched Employees; 1982 Self-Regulating Rules; 1982 Promotion Council; 1984 Self-Regulating Standards; and 1987 Retail Code.

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-With respect to a single measure¹¹¹ (which was published nine days before the conclusion of the Kennedy Round), the date of publication was not determinative.

iii) Upsetting (nullifying or impairing) the competitive relationship - causality:¹¹²

The third required element of a non-violation claim under Article XXIII:1(b) is that the benefit accruing to a WTO Member (e.g., improved market access from tariff concessions) is *nullified or impaired as the result of* the application of a measure (not reasonably anticipated) by another Member. According to GATT/WTO panel practice, a complaining party had to demonstrate a clear correlation between the measures at issue and an adverse effect on the relevant competitive relationship between domestic and like foreign products. (para. 10.82)

Most past non-violation cases dealt with situations where a GATT-consistent domestic subsidy for the producer of a product had been introduced or modified in accordance with the grant of a tariff concession on that product. Whether assistance was financial or non-financial, direct or indirect, did not determine the issue as to whether its effect did in fact offset legitimate expectations accruing to a Member from tariff concessions.

In the present case, the competitive relationship between domestic and imported film and paper *at the time* when market access was improved through a tariff concession had to be compared with the competitive relationship between domestic and imported products *after* the introduction of the measures at issue. The purpose of the non-violation remedy is to prevent an existing *competitive relationship* between domestic and imported products from worsening, while in the case of a violation

¹¹¹It is 1967 Cabinet Decision which was published on 21 June 1967. Note that the Kennedy Round was concluded on 30 June 1967.

¹¹²The Panel considered that this element (causality) may be one of the more factually complex areas of its examination of a non-violation claim: in three past GATT panel cases, the complaining parties failed to provide a detailed justification to support their claim (i.e., Uruguayan Recourse, **BISD 11S/95**, 100, para. 15; Japan - Semiconductors, **BISD 35S/116**, 161, para. 131; U.S. - Agricultural Waiver, **BISD 37S/228**, 261-62, paras. 5.20-5.23.

claim against less favourable treatment (e.g. under national treatment clause), its remedy is to ensure *the equality* of competitive opportunities of imported and domestic products.

Even if competitive relationships had changed to the detriment of imports, it still needed to be demonstrated that this adverse effect had been caused by measures in dispute. In previous cases, as mentioned, complainants often failed to establish non-violation claims due to lack of evidence of causality. Regarding the requisite degree of causation, the Panel considered that a complainant need not show the measure at issue "but for" causes for impairment of market-access conditions for imported film and paper. Furthermore, the Panel did not accept the view that a complainant need only demonstrate that measures were, among others, "a" cause of such distortion. It did not matter for the Panel whether market intervention attributable to the government was a necessary condition for the emergence of vertical integration that prevented market penetration by foreign products, nor whether governmental intervention merely supported the development of single-brand distribution which private market forces would have created even in the absence of any governmental intervention.

Accordingly, the Panel concluded that Japan should be responsible for what was caused by measures attributable to its government as opposed to what was caused by restrictive business conduct attributable to private economic participators. In the Panel's view, the issue was whether the measures had caused individually or collectively more than a *de minimis* contribution to nullification or impairment. (para. 10.84)

a) Distribution measures

The gist of the U.S. claim in respect of distribution measures was that Japan had created vertical integration between manufacturers, primary and secondary wholesalers and retailers, and single-brand distribution in the Japanese film and paper market. Japan responded that such vertical integration and single-brand

wholesale distribution predated the measures cited by the U.S. and therefore could not be caused by these measures. In addition, Japan also contended that single-brand distribution was the common practice in the photographic materials market in most countries including the U.S. (para. 10.204)

The Panel found a fundamental flaw in the U.S. claim., namely, vertical integration and single-brand wholesale distribution predated the measures cited by the U.S. Accordingly, because of the timing issue, the Panel found that the U.S. had been unable to prove how the measures challenged by the U.S. could have caused vertical integration. (para. 10.204)

Furthermore, the Panel noted that proof of an underlying intention to nullify or impair of benefits was not required under Article XXIII:1(b). The Panel therefore found that the intent of a measure was irrelevant. Instead, what was relevant for showing causality was *the actual impact* of a measure. The Panel also considered the issue of potential effects, whether procompetitive or anticompetitive, of single-brand distribution in the Japanese film market. In the view of the Panel, this issue was irrelevant for the purpose of examining whether the competitive relationship between domestic and imported products had been upset as a result of distribution measures attributable to the Japanese government. (paras. 10.206, 10.208)

b) Large stores law

Concerning measures restricting the opening of large scale retail stores, the main issue was whether large stores were more likely to sell imported film, and whether Japanese regulation of large stores was currently stricter than in 1967, 1979 and 1993.

The Panel noted that neither U.S. nor Japanese studies were conclusive, i.e. U. S. studies demonstrated that stores with large floor *space* were more likely to carry imported film, while Japanese studies demonstrated that stores with a high *volume* of sales were more likely to carry foreign film. (paras. 10.212, 10.213)

The Panel limited itself to a finding that the U.S. had not been able to demonstrate that the Japanese regulation of large stores was currently more restrictive than in 1967, 1979 or 1993. Accordingly, the U.S. failed to establish that its legitimate expectations about competitive relationships in the film market had been denied. (para. 10.232)

c) Promotion measures

The U.S. claim regarding the measures affecting the promotion of products was that, the restrictions on promotional methods technically applied *de jure* equally to Japanese and U.S. film producers. In actuality, however, these restrictions prevented U.S. film imports *de facto* from challenging the allegedly entrenched Japanese film market. Japan responded that only a few kinds of promotional methods were restricted. Nonetheless, the basic tools of promotion, such as truthful advertising and price competition, remained open.

In the view of the Panel, the measures at issue could have had a disparate impact on imports although they were neutral in terms of the origin of products. Nevertheless, the U. S. failed to demonstrate any single instance where the implementation of the promotion measures had affected the competitive relationship between imported and domestic film and paper in the Japanese market. In the Panel's view, the U.S. only demonstrated that a few kinds of promotional methods were restricted, such as false advertising, and certain premiums for customers. Other basic promotion methods, however, such as truthful advertising and price competition, remained open. Accordingly, the Panel found that the U.S. had failed to demonstrate that these basic tools could not be utilised effectively in the Japanese market. (para. 10.349)

d) Combination Effect

As to the combined effect of the three different measures examined above, (i.e., distribution, large store and promotion measures), the Panel noted that it was not implausible that individual measures which did not impair benefits when considered in *isolation*, could nonetheless have an adverse impact on conditions of competition

when considered *collectively* ("nothing combined with nothing is still nothing"). The Panel, however, found that it was incumbent on the U.S. to provide this Panel with a detailed demonstration of the complementary and cumulative effects of these measures, acting in combination, on film and paper (i.e., how they interacted with each other in their implementation so as to cause effects different from, and additional to, those effects which were alleged to be caused by each measure acting individually). The Panel concluded that the U. S. had failed to demonstrate such an impact. (para. 10.353)

To sum up, the Panel found that none of these measures, either individually or collectively, had upset the competitive relationship between imported and domestic products.

3. Violation claims

i) National treatment clause

Apart from a non-violation claim, the U.S. further argued that the distribution measures were inconsistent with the requirement of national treatment under GATT Article III:4

a) "Laws, regulations and requirements"

The Panel noted that a broad reading had been given in the previous GATT/WTO cases to the terms "laws, regulations and requirements" in Article III:4. The Panel concluded that these terms should be given an interpretation similar to the term "measure" found in Article XXIII:1(b). (paras. 10.374, 10.375, 10.376)

In consequence, along with its findings regarding the governmental attributability of "measures" for non-violation claims, the Panel found that 3 distribution measures¹¹³ constituted "requirements" in Article III and might still be effective, while 1 measure¹¹⁴ was no longer in effect. The other 4 distribution measures¹¹⁵ were found

¹¹³The three distribution measures were: (i) 1967 Cabinet Decision; (ii) 1970 Guidelines; and (iii) 1971 Basic Plan.

¹¹⁴It was 1967 JFTC Notification 17.

not to be attributable to the Japanese government and thus did not fall within the scope of Article III. (para. 10.377)

b) Less favourable treatment

Furthermore, the Panel concluded that the U.S. had failed to demonstrate that the distribution measures accorded less favourable conditions of competition to imports than to domestic film or paper in the Japanese market. The Panel was unconvinced that there was a meaningful nexus between the distribution measures (i.e. the 1967 Cabinet Decisions or the 1970 Guidelines) and the largely pre-existing system of single-brand distribution which was a common market structure in most major national film markets including the U.S. In addition, in the Panel's view, the recommendations of the 1971 Basic Plan appeared to have been neutral as to the source of products, promoting the standardisation and modernisation of business practices and management techniques, including computerisation. (para. 10.381)

ii) Publication of administrative rulings of general application

As for another violation claim, the U.S. made a further claim under GATT Article X which required that administrative rulings of general application had to be published. The U.S. argued on the following points in particular: (i) unpublished enforcement actions by the JFTC and fair trade councils under the Premiums Law and relevant fair competition codes that established or modified criteria applicable in future cases; and (ii) unpublished guidance through which the Japanese authorities (i.e. regional MITI offices, prefectural government and local authorities) made applicants for new or expanded large stores co-ordinate their plans with local competitors before submitting a notification for government review, and continued to impose a "prior explanation" requirement inconsistent with Article X:1. (para. 10.383)

Although the Panel accepted the notion that not only administrative decisions of general application needed to be published, but also individual decisions that

¹¹⁵These were: (i) 1968 Sixth Interim Report; (ii) 1969 Seventh Interim Report; (iii) 1969 Survey; and (iv) 1975 Manual.

established or modified criteria applicable in future cases. The U.S. had not been able to demonstrate any criteria applicable to future cases which these individual decisions established or modified (i.e. the U.S. simply cited a great number of unpublished individual decisions). (para. 10.401)

Remarks on the case:

The present case represented an important but difficult challenge for the WTO. For example, it went beyond the jurisdiction of traditional GATT dispute issues, namely, issues with respect to domestic distribution structures and private business practices. Furthermore, the issue dealt more broadly with market access and the international dimension of competition. Besides, the following points are worth noting:

(i) Non-violation claims: its limitation and the risk of expanded application

The Panel ruled that:

- government measures other than subsidies, including distribution measures, could be used to prove a nullification and impairment case;
- "measures" within the meaning of Article XXIII can include not only a formal law or regulation but also guidance, such as administrative guidance of the kind utilised by Japanese government.

The Panel affirmed, as in the past, in its findings the limited, exceptional and supplementary nature of non-violation complaints. The Panel noted that there had only been eight cases¹¹⁶ of referrals regarding non-violation complaints during the whole history of GATT. This record shows that the GATT contracting parties and WTO Members had regarded non-violation claims as exceptional cases.

The U.S., nonetheless, sought for an expansion of the scope of non-violation complaints in the present case. The Panel maintained the strict requirements that had been applied in previous cases, i.e. the complainants had the burden of presenting a

¹¹⁶Of eight, in five cases in which the Panel/Working Party upheld the non-violation claim. Of five, three reports of Panel/Working Party were adopted, see cases marked with asterisks in, *supra* note 92.

detailed justification in support of their claims, and showed that when measures themselves were *de jure* non-discriminatory, a detailed demonstration of the relationship between measures and goods would have to be provided to support complaints. As indicated in the past GATT cases, the panels have allowed non-violation complaints in which there was clear evidence that the introduction of measures at issue by the government had distorted the competitive conditions for imports, for example, such measures relating to subsidies and tariffs associated with specific goods.¹¹⁷

Another point to be noted is that the scope of WTO agreements was extended after the Uruguay Round. This means that it narrowed the supplementary functions of non-violation complaints (which had been designed to address measures not covered by the GATT, for instance, competition policy). Accordingly, a difference was further clarified between violation and non-violation complaints to the DSU. For example, non-violation complaints did not constitute a *prima facie* case of nullification or impairment (Article 3:8); and non-violation complaints required a complaining party to present a detailed justification in support of its complaint (Article 26:1(a)).¹¹⁸

With respect to remedies of non-violation complaints, if such complaints are upheld, there is no obligation to withdraw the measure (unlike a violation case). Instead, a mutually satisfactory adjustment is made.¹¹⁹ If no such adjustment is reached, retaliatory measures may be invoked (just as for violation claims).¹²⁰

¹¹⁷There are some examples of non-violation claims that tried to ignore the limitations, though they set dangerous precedents in terms of the expanded application of non-violation claims. Accordingly, they were unadopted. See, the EC citrus case, *supra* note 92.

¹¹⁸For other agreements that defines the exceptional nature of non-violation complaints, see, for instance, Article 64:2 of the TRIPs Agreement, which prescribes that "Subparagraphs 1(b) and 1(c) of Article XXIII of GATT 1994 *shall not apply to the settlement of disputes under this Agreement for a period of five years from the date of entry into force of the WTO Agreement (emphasis added)*."

¹¹⁹Article 26:1(b) DSU.

¹²⁰See, *ibid.*, Article:1(d).

In the meantime, one should be aware of the danger that an expanded interpretation of what constitutes non-violation complaints would mean that countries might have to pay compensation even though they applied measures which were not in violation of the Agreement (for example, "compensation may be a part of mutually satisfactory adjustment"¹²¹). It would be equivalent to allowing tariff concessions to be altered without any formal negotiation, which would not only undermine legal stability but also damage the credibility of concession negotiations.

(ii) Limitation of jurisdiction in the WTO rule: trade and competition

As mentioned earlier, the dispute concerning the Japanese film market had been initiated in May 1995 by Kodak's complaint to the USTR under Section 301 of the 1974 Trade Act alleging that it was unfair and irrational for Japan to permit anticompetitive practices engaged in by Fuji Photo Film involving the Japanese consumer photographic film and paper market. Nonetheless, unlike previous patterns of behaviour, Japan did not agree to enter into bilateral consultations under Section 301. In Japan's view, Kodak's complaint was essentially regarding the administration of Japanese Anti-monopoly Law and was therefore unsuitable for bilateral negotiation. Instead, this claim should have been made directly to the Japan Fair Trade Commission (JFTC) (which concluded an investigation in July 1997 by finding that there was no violation of the Anti-monopoly Law).

As is already known, the issue of competition has not yet been included within the WTO's jurisdiction. In the meantime, the Working Group on the Interaction between Trade and Competition Policy (established in 1996 at the WTO Singapore Ministerial Conference) will issue a report on trade and competition.¹²² Meantime,

¹²¹*Ibid.*

¹²²The U.S., Japan and Korea presented papers to the meeting (July 27-28 1998) of the WTO competition policy working group. Both Japan and Korea stated in their paper that antidumping could be reformed to incorporate the principles of competition policy. See for further detail of each papers submitted to the Working Group, i.e., Japan Paper for the Fifth Formal Meeting of the Working Group on Interaction between Trade and Competition Policy, 27 July 1998; Impact of Trade Policy on Competition: An Assessment of Anti-Dumping Rule (Communication from Republic of Korea), 27 July 1998; Korea's Intervention on Agenda Item II(b): Impact of Trade Policy on Competition; Observations on the Distinctions Between Competition Laws and Antidumping Rules (Submission of the U.S.

the Joint Group on Trade and Competition in the OECD is also working on this issue in order to clarify the relationship between trade and competition policies.¹²³

(iii) Procedural ambiguity of remedies in cases of non-violation claims

No provision covers anti-competitive policies and practices in the WTO Agreements. Nonetheless, GATT Article XXIII provides for remedies for non-violation nullification and impairments.

As had been the case in the past panels, "non-violation complaints" were resorted to only in exceptional cases. It is further noted in Article 26:1(a) of the DSU that a complainant must present a detailed justification in support of its complaints. The remedies sought by the U.S. in this case (i.e. seeking the Japanese government to take measures to eliminate "anticompetitive practices" that had developed in its distribution system as a result of measures that were no longer in effect) would be exceeding the bounds of the current WTO DS system and constitute an additional or reduction of obligations under the Agreement, which could be in violation of Article 19:2 of the DSU.¹²⁴ Eventually, the Panel did not reject the substance of the U.S. claim on technical or procedural grounds but instead, the Panel found against the U.S. on the fundamental issues of factual evidence.

for the Working Group meeting of 27-28 July 1998); Impact of Trade Policy on Competition (Submission of the U.S.); The Impact of Regulatory Practices, State Monopolies, and Exclusive Rights on Competition and Internal Trade (Submission from the U.S.), see also "Korea, Japan Seek Changes to Dumping Laws to Allow More Competition", Inside US Trade, 21 August 1998; see also the communication from the European Community and its member states, WT/WGTCP/W/78 (7 July 1998); see generally, "Report (1988) of the Working Group on the Interaction Between Trade and Competition Policy to the General Council", WT/WGTCP/2 (8 December 1998).

¹²³See, in general, OECD, Strengthening the Coherence Between Trade and Competition Policies - Joint Report by the Trade Committee and the Committee on Competition Law and Policy, OECD/GD(96)90, Paris, 1996; OECD, The Scope, Implication and Economic Rationale of a Competition-Oriented Approach to Future Multilateral Trade Negotiations, TD/TC(96)6, Paris 15 February 1996 (derestricted on 22 April 1996); OECD, Trade and Competition Policies, OECD/GD(94)63, Paris, June 1994; OECD, Trade and Competition Policies, OECD/GD(93)10, Paris, June 1993.

¹²⁴Article 19:2 DSU prescribes that "..., the Panel and Appellate Body cannot add to or diminish rights and obligations provided in the covered agreements."

One may argue that in the case of complaints on new issues such as anticompetitive practices, perhaps it would be an alternative for a complainant, for example, to require exhaustion of local remedies before initiating a panel proceedings at the WTO. Otherwise, the WTO would be faced with the danger of increasing complaints in relation to new complexed issues such as competition which are beyond the current WTO jurisdiction. This may eventually undermine the WTO DS mechanism.

(iv) Rule-oriented trade policy to be re-affirmed

The Panel showed its support for a rule-oriented trade policy in the present dispute. The U.S. perception that the "Japanese market is closed", was used to justify its claims in the dispute. The Panel, however, judged this case based upon the arguments and evidence presented to it after extensive tests as to whether the U.S. claims satisfied the requirements of the WTO rules. This impartial as well as objective attitude should be supported in order to give further credibility to the DS system and support WTO Members' confidence in the multilateral DS mechanism available from the WTO.

(v) The U.S. reaction to the Panel ruling

The U.S. complaint regarding the Japan - film issue was very much factual based because the issue centred on convincing a panel that Japan did in fact seek to close its markets to imports. As a result of this being a factual-based claim, the U.S. have refrained from appealing because WTO appeals have to be limited to "issues of law" comprised in the panel report and to legal interpretations of the WTO Agreements.¹²⁵ The U.S. decided not to appeal, which lead us to be reminded of a provision which states that a report unappealed shall be deemed to be adopted unless the DSB decides by consensus not to adopt the appeal.¹²⁶ The U.S. therefore adopted the Panel's ruling.

¹²⁵Article 17:6 DSU.

¹²⁶Articles 16:4 and 17:14 DSU.

Instead, the U.S. however decided that it would regard Japanese representations made by the Japanese government at the panel on the openness of the Japanese market to constitute formal "commitments". To that end, the U.S. government established an inter-agency Monitoring and Enforcement Committee to review implementation of formal representations made by the Japanese government to the WTO panel regarding its efforts to ensure the openness of its market to imported film. In the view of the U.S., Japanese representations made to the WTO by the Japanese government should ensure the openness of its market. In this respect, Japan informed the U.S. that it would not cooperate with the U.S. on this new effort ("initiative").¹²⁷ Under current WTO rules, no provisions define such a notion, i.e. representations which are made by a party to the WTO panel will constitute "commitment" to certain obligations. In other words, representations to a panel are seen by Japan more as individual "efforts" by a party. It seems that this U.S. strategy is akin to demands with threats for the removal of impediments.

In the meantime, however, despite the panel's ruling favourable to Japan, the Japan Fair Trade Commission (JFTC) has begun two new surveys to determine whether anti-competitive practices were hindering market access in Japan for film and photographic paper (and also flat glass). In addition, Japanese advisory industry councils agreed with the U.S. to the elimination of a law regulating the establishment of large stores as part of a deregulation initiative agreed in 1997 between Japan and the U.S.

On 19 August 1998, the U.S. government (USTR) released the first semi-annual monitoring report on Japan's film market.¹²⁸ One may foresee potential dangers behind such a report. That is, in the event that Japan does not ensure the openness of

¹²⁷"House Calls on Japan to Open Market For Film, Other Sectors", Inside US Trade, 13 March 1998, p. 1.

¹²⁸The first semi-annual Monitoring Report on foreign access to Japan Film, titled "USTR Report on Japanese Film" was issued on 19 August 1998, the reproduction of the report is available in Inside US Trade, also see "U.S. Calls for Increased Japanese Efforts on Film Market Access", Inside US Trade, 21 August 1998; So far, since the result of this monitoring showed some progress in several areas related to market access for foreign film. The next report will be released in early 1999.

its market, another dispute may arise or even unilateral sanctions may be imposed. If this happens, this new type of U.S. programme could hinder or even undermine the progress of the WTO DS system.

(vi) Criticisms of the report

In a letter to the USTR office, Dewey Ballentine, a lawyer representing Kodak, alleged that "*most of the decisions in the case were not made by the three-strong panel but by the WTO secretariat 'who lacked both the competence and the mandate to do so'*".¹²⁹ Nonetheless, responsibilities of the Secretariat are limited, as prescribed in Article 27:1 DSU, to assist panels in respect to "legal, historical and procedural aspects" of cases. Furthermore, in order to fulfil these requirements, the Secretariat provides secretarial and technical support to panellists. Accordingly, the decision of the present case must have been made by the panel as in other cases.

To my knowledge, through my internship at the WTO Secretariat, the above accusation seems to be unfounded. The report drafting is normally conducted by the panel and further the Legal Affairs and operational divisions (components of the Secretariat service assisting a panel) do not necessarily share the same opinion towards the issues.¹³⁰ Nonetheless, objectively, one can not rule out the possibility that a particular panel might exceptionally be Secretary-driven. For example, from my own limited observation, one might assume that the influence of the Secretariat could be stronger in cases where both the Legal Officer and Panel Secretary are provided by one division, for instance, the Legal Affairs or Rules Division.¹³¹ Nonetheless, no definite basis for such an allegation exists at this stage.

¹²⁹The Financial Times, "Kodak attack on handling of WTO case", 7 July 1998 at 7.

¹³⁰Ichiro, Araki., "*WTO ni okeru funshoshori no jissai*" [The reality of dispute settlement in WTO (translated by myself)], 46 Boueki to Kanzei (no. 9), September 1998 at 31.

¹³¹So far, there are three cases in which only the Legal Affairs Division has been involved (i.e. providing both Panel Secretary and Legal Officer/Legal Advisor). Those cases are: the three Alcohol cases involved three countries respectively Japan (WT/DS8/R; WT/DS10/R; WT/DS11/R), Korea (WT/D75/R; WT/DS84/R, these report was issued on 31 July 1998 and its appellate report was out on 18 January 1999, WT/DS75/AB/R; WT/DS84/AB/R), Chile (WT/DS87/...; WT/DS110/..., which are still on); Japan - Film case (WT/DS44/R); the Argentina - Footwear case (WT/DS56/R). While, note that only the Rules Division gets involved in cases on Dumping and Subsidies. Nonetheless, even in such a case, the Director of Legal Affairs Division normally attends at an internal meeting but not at a formal panel

meeting. According to a Legal Officer of WTO, there is one new development, that is, as for cases concerning Safeguards, both Rules and Legal Affairs Divisions are involved.

GENERAL CONCLUSION

"We must take the responsibility for the life of all men, and develop on an international scale what all great countries have developed internally, a relative sharing of wealth and a new and more just division of economic resources. This must lead eventually to forms of international economic co-operation and planning, to forms of world government".¹

In the last fifty years, the GATT/WTO Dispute Settlement ("DS"), due to the commitments and efforts of the contracting parties, has been progressively judicialised.

In line with the institutional and constitutional developments of the GATT/WTO, Japan's trade policy towards DS has also gone through significant changes. The most striking feature of this change is a shift from what I call "bilateralism" to "multilateralism";² that is a transformation from a political/power-oriented to a more judicial/rule-oriented approach in resolving disputes.

The above two themes constitute the main focus of this work.

The judicialisation process has been most prominent with regards to the institutional aspects of the GATT/WTO. There has been, for example, the introduction of the "panel" procedure, the establishment of the Legal Affairs Office at the GATT Secretariat in 1983 and more recently the creation of the General Council (which transforms itself, as needed, into the Dispute Settlement Body and the Trade Policy Review Body) and a second tribunal, the Appellate Body ("AB").

While, similar developments could be noted in the constitutional sphere, with respect to the DS system, among a number of events discussed in this thesis, perhaps one of the most important turning points in the history of GATT could be the Tokyo Round

¹Fromm, Erich., *The Sane Society*, 2nd ed., Routledge, London, 1992 at 360.

²See, for instance, significant cases in terms of the "transformation", such as the Semiconductor case (Section 7.1.1.4. in Chapter 7 of the thesis) and the Auto and Auto Parts dispute (Section 8.1.1.1. in Chapter 8 of the thesis).

("TR") Agreements which contained a set of provisions dealing with the DS (the "Understanding").³ Moreover, this has provided a detailed procedure of the DS system, and it eventually became the basis of the DSU which constitutes an integral part of the WTO Agreement. The further developments in the area of DS subsequent to the TR emerged in later documents, which are examined in Chapters 2 and 5, such as the 1984 Action on DS, the Leutwiler Report (1985), the 1989 Improvements (i.e. the Mid-Term Review), the Dunkel Draft (1991), and, above all the DSU of the WTO Agreement (1994).

There is no doubt that the DS system is more effective, efficient and predictable under the new WTO system. As explained at the outset of this study, there were a number of defects under GATT, for instance, a country against which the complaint has been made might have delayed the DS process at various stages. Delays occurred especially in the forming of a panel and also in the adopting of a panel report. The major cause of delay was the consensus rule (i.e. the consensus of all countries present in the meeting where the matter was being considered). Whereas, as has been explained in Chapter 5, now it is almost impossible to delay the process under the new DS rules, because the decisions are almost automatically made (e.g. in establishing a panel, in adopting a report of a panel) except if there is a negative consensus. Furthermore, by the introduction of the stringent time-frame at various stages of the DS process, an undue delay has been effectively eliminated.

However, this does not mean that all those defects in the system were totally eliminated. In fact, the DS system still may not be quite perfect; certain shortcomings of the new system are emerging, for example, an issue of implementation which is apparently under discussion in the ongoing *Banana* dispute.⁴ In this dispute, the different views between the EU and the U.S. legal

³Understanding Regarding Notification, Consultation, Dispute Settlement and Surveillance, adopted on 28 November 1979, **BISD 26S/210**; also see, in general, Section 2.4.1.5. in Chapter 2 of the thesis.

⁴In the *Banana* case, the period for implementation was set by arbitration at 15 months and a week from the adoption of the reports, i.e. the expire date is on 1 January 1999, WT/DS27/15 (7 January 1999). The EC has undertaken to comply with the DSB's recommendations within

interpretations arise from lack of clarity in the DSU procedures due to the ambiguous DSU language. For instance, the way how to implement recommendations of the panel or AB is prescribed in Article 19.1 of the DSU which provides "... , the panel or Appellate Body *may suggest ways* in which the Members concerned could implement the recommendations" (emphasis added). For this reason, the Panel viewed that such suggestions on implementation are not part of the recommendation, and are not binding on the Member affected.⁵ In fact, so far, panels have been somewhat reluctant to suggest specific ways and means on how to implement their

the implementation period. The complainants requested consultations with the EC for the resolution of the disagreement between them over the WTO-consistency of measures being proposed by the EC in purported compliance with the recommendations and rulings of the Panel and AB. At the DSB meeting on 25 Nov. 1998, the EC announced that it had adopted the second Regulation to implement the recommendations of the DSB, and that the new system will be fully operational from 1 January 1999. The complainants have expressed their dissatisfaction with the WTO-consistency of the new system and consultations are continuing between the two sides to this dispute. On 15 December 1998, the EC requested the establishment of a panel (under Article 21.5 of the DSU) to determine that the implementing measures of the EC must be presumed to conform to WTO rules unless challenged in accordance with DSU procedures [WT/DS27/40 (15 December 1998)]. On 18 December 1998, Ecuador requested the re-establishment of the original panel (pursuant to Article 21.5) to examine whether EC measures to implement the recommendations of the DSB are WTO-consistent [WT/DS27/41 (18 December 1998)]. At its special meeting on 12 January 1999, the DSB agreed to reconvene the original panel (pursuant to Article 21.5) to examine both Ecuador's and EC's requests [WT/DS27/44 (18 January 1999), WT/DS27/44/Corr.1 (26 January 1999) and WT/DS27/45 (18 January 1999), WT/DS27/45/Corr.1 (25 January 1999) respectively]; see the Communication from Guatemala, Honduras, Panama and the United States on European Communities - Regime for the Importation, Sale and Distribution of Bananas, WT/DS27/42 (12 January 1999); the Financial Times, "WTO orders review but fails to cool temper", 13 January 1999 at 4; the Financial Times, "US seeks WTO backing for sanctions in banana war", 15 January 1999 at 5; see for the U.S. request for authorisation to suspend the application to the EC (and its member states) tariff concessions and related obligations under the GATT 1994, covering trade in an amount of US\$520 million, WT/DS27/43 (14 January 1999); the Financial Times, "EU appeals to WTO over US threat of trade sanction", 22 January 1999 at 5; *ibid.*, "Island growers spike US sanctions move", 26 January 1999 at 6; *ibid.*, "Trade goes bananas", "Cappinig CAP", 26 January 1999 at 19; *ibid.*, "US augments weaponry for trade disputes", 27 January 1999 at 6; *ibid.*, "Italians urge EU to retreat in banana dispute with the US", 27 January 1999 at 6; *ibid.*, "Sanctions threat starts to tell", 27 January 1999 at 6; *ibid.*, "Yellow peril", 27 January 1999 at 23; see also Request for Consultations by Honduras, Mexico, Guatemala, Panama and the United States, WT/DS158/1; G/L/290; S/L/65; G/LIC/D/27 (25 January 1999); Request for Joint Consultations by Ecuador, WT/DS158/2 (27 January 1999); for the summary of the 25 January week concerning the Banana dispute (since the 25 January DSB meeting whose agenda was blocked by St. Lucia and Dominica), see Inside US Trade, 29 January 1999; the Financial Times, "Exporters apoplectic at being placed in bananas firing line", 29 January 1999 at 5.

⁵See, para. 8.2 in the report of the Panel on Guatemala - Anti-Dumping Investigation Regarding Portland Cement From Mexico, WT/DS60/R (19 June 1998); also see the first sentence of Article 19.1 of the DSU.

recommendations. Usually they give what seems to be a declaratory judgement on what is consistent or inconsistent and leave the countries concerned the leeway to choose mechanisms for compliance. However, panels are becoming aware that they should be more precise so as to facilitate implementation.⁶ Under the new WTO system, the novelty however is that there is a procedure of reconvening the original panel to check whether compliance was full or merely partial,⁷ and furthermore there are provisions concerning compensation and retaliation.⁸ One can therefore say that there is indirect or political pressure to implement more or less fully. In any event, the *Banana* dispute seems to be an emerging opportunity for clarification of the ambiguous implementation procedure. If it turns sour, however, it could become a prelude to breakdown the whole WTO system.

⁶With regard to "suggestions on implementation" by the Panel/AB under Article 19.1 of the DSU, see, para. 8.3 in the report of the Panel on United States - Restrictions on Imports of Cotton and Man-Made Fibre Underwear, WT/DS24/R (8 November 1996), which stated "[The Panel] further suggest that the United States bring the measures challenged by Costa Rica into compliance with US obligation ... by immediately *withdrawing* the restriction imposed by the measure" (emphasis added); regarding the same aspect, see also, para. 8.6 in the Panel report on *Guatemala Cement* case, WT/DS60/R, *supra* note 5, which stated that "[The Panel] suggest that Guatemala *revoke* the existing anti-dumping measure on imports of Mexican cement, ..." (emphasis added); cf. the awareness of the Panel regarding "suggesting ways to implement" in recent reports, for example, the report of the Panel on India-Quantitative Restrictions on Imports of Agriculture, Textile and Industrial Products, WT/DS90/R (6 April 1999), Section VIII (Suggestions for Implementation), which provided a detail suggestion, in my view, which will certainly help to prevent facing to a future dispute over implementation between the parties concerned. The prolonged dispute over implementation in the *Banana* dispute might have lead to such an awareness of the Panel in the India RQs case. (cf. Section F "Suggestions on Implementation" in the Ecuador claim recourse to Article 21.5 of the DSU over *Banana* dispute, with respect to GATT Articles I and XIII, the requirements of the Lomé Convention and the coverage of the Lomé waiver, suggested three options for bringing the EC *Banana* import regime into conformity with WTO rules. However, no specific suggestions in respect of licence allocation were made. The report noted, though, "licences would not be needed at all in a tariff-only regime".); see further, in particular, Section VII. in the report of the Panel on U.S. - Anti-Dumping Duty on Dynamic Random Access Memory Semiconductors (DRAMs) of One Megabit or Above from Korea, WT/DS99/R (29 January 1999), the Panellist simply said that "However, in the light of the range of possible ways in which we believe the U.S. could appropriately implement our recommendation, we *decline to make any suggestion* in the present case." (emphasis added) which clearly shows the reluctance of the Panel to suggest means in this case.

⁷Cf. In the *Banana* dispute, the Ecuador's panel request for re-establishment of the original panel to consider and verify whether the DSB recommendations have been effectively implemented by the EC (Article 21.5 of the DSU), and to suggest to the EC how to implement its findings (Article 19.1 of the DSU), WT/DS27/41, *supra* note 4.

⁸See, *ibid.*, Article 22; cf. the U.S. claim in the *Banana* dispute.

In parallel to the GATT/WTO evolution, Japan has transformed its trade policy on DS in order to be more in tune with the nature of the new WTO DS system, i.e. multilateralism: Japan now follows a more rule-oriented or quasi-judicial approach at the multilateral table (WTO) in resolving trade disputes.⁹

To start with, it should also be noted that Japan's contribution towards the development of the present DS mechanism of the WTO has been significant not only in terms of its involvement in the UR negotiations but also in terms of its willingness to take part and indeed abide by the findings of the panels and appellate bodies' recommendations.¹⁰ For example, as examined in Chapter 3, we should recall that by far the largest contribution made by Japan in the area of DS during the UR negotiations was its insistence on the inclusion of a provision regarding prohibition of unilateral measures, particularly the U.S. Section 301. As the result of its insistence on this point, Article 23 of the DSU was adopted. Indeed, the inclusion of this provision in the new DS system (DSU) was crucial for Japan (and some other countries) which had been the target in many occasions of Section 301. In recent cases (e.g. the *Auto and Auto Parts* dispute,¹¹ the *Film* case,¹² the *Indonesian National Car* case¹³) Japan has already shown its multilateral approach in resolving its dispute under WTO. However, a serious assessment of Japan's commitment to

⁹See, Appendix II to the thesis; the current trend of Japanese policy regarding DS could be recognised under the column titled "Japan's attitude: a current pattern" in this appendix. In short, Japanese involvement in disputes is based more on a multilateral, legal and rule-oriented approach.

¹⁰Japan also made a series of proposals regarding substantive issues (which included safeguards, subsidies and countervailing measures, the TR Codes, such as anti-dumping, standards, import licensing, customs valuation, government procurement and subsidies). In addition, it was the meeting in Tokyo* convened at the instance of Japan, which was instrumental in the re-launching of the negotiations, especially when the UR negotiation were held up in the early half of 1993. Furthermore, Japan also showed its contribution in other areas, such as, market access, trade in services, agriculture and so on. In short, success of the UR negotiation was achieved not by a particular member's contribution but by the accord of all member states collectively, including Japan.

*Before the Tokyo Economic Summit held on 7-9 July 1993, on the eve of the summit on 7 July 1993, the Quadilateral Trade Ministers (the United States, the European Community, Japan and Canada) announced a substantial market-access agreement that enabled re-engagement in the Uruguay Round negotiation; for the text of the announcement of 7 July 1993, see GATT, GATT Focus, No. 101, August-September 1993.

¹¹See, Section 8.1.1.1. in Chapter 8 of the thesis.

¹²See, Section 8.1.2.2. in Chapter 8 of the thesis.

¹³For the summary of the case, see Appendix III of the thesis.

multilateralism would be in a dispute in which Japan is a loser (e.g. the *Alcohol-II* case,¹⁴ the *Japan "Apple"* case¹⁵). It is therefore significant to see how Japan implements the recommendations of Panel/AB in accordance with the DSU.

From the case studies, one can speculate as to why Japan has transformed its attitude towards DS under GATT/WTO:

1) The new Japan's policy on DS favouring a "multilateral"/"rule-oriented" approach emerged after experiencing defeats in four successive cases¹⁶ during the 80's. In other words, these "defeats" may have propelled Japan to shift its approach towards DS from a "bilateral" to a "multilateral" one under the GATT(WTO) system.¹⁷ Among other cases, as examined in Chapter 7, the defeat experienced at the *Semiconductor* case became a decisive one for Japan to change its policy on DS. Japan realised that bilateralism is no longer an optimum solution for securing settlement.

2) Japan's arguments during the panel proceedings seemed to become more legal and technical. As demonstrated through the case studies,

¹⁴See, the 3rd status report of Japan, pursuant to Article 21(6) of the DSU, titled, Status Report by Japan on Implementation of the Recommendations and Rulings of the DSB regarding "Japan - Taxes on Alcoholic Beverages", WT/DS8/18/Add.2; WT/DS10/18/Add.2; WT/DS11/16/Add.2 (7 November 1997); also see the Japan's communication (dated 9 January 1998) between Japan and the U.S. titled, Mutually Acceptable Solution on Modalities for Implementation (regarding Japan - Taxes on Alcoholic Beverages), WT/DS8/19; WT/DS10/19; WT/DS11/17 (12 January 1998); also see the communication between Japan and Canada under the same title as the previous document, WT/DS8/20; WT/DS10/20; WT/DS11/18 (12 January 1998).

¹⁵See, for the summary of the case in Appendix III to the thesis; this case was appealed on 24 November 1998 (WT/DS76/5) and the report of the AB is expected to be out at the end of February 1999.

¹⁶In 1984, the GATT panel ruled that Japanese measures on import of leather violated GATT rules. In addition, during the period 1987-88, a GATT panel judged that Japan violated GATT rules in three cases. These cases are: Alcohol-I case in 1987; Agricultural Products case in 1988; Semiconductors case in 1988. For those cases, see Section 7.1.1. in Chapter 7 of the present thesis. For Japan, after that difficult period, a more active usage of the dispute settlement procedure under GATT rules (i.e. multilateral approach) was gaining importance.

¹⁷See for this case, Section 7.1.1.4. in Chapter 7 of the thesis; As seen from this study, the conventional Japanese way to resolve trade disputes had been, for a long time, mainly by "bilateral" approach (utilising less legal and relying on more political approach; perhaps, it was partly due to its long non-litigious legal tradition, namely, Japan preferred non-judicial means of settling disputes).

more technical and legal arguments were put forward by Japan, in particular, in recent cases. Whereas, in the old cases, particularly in the *Agriculture* case,¹⁹ the *Leather* case,²⁰ and the *Alcoholic Beverages* case,²¹ Japan made less legal or technical, (i.e. irrelevant) arguments in its defence. For instance, Japan relied on to its own domestic "social and cultural" reasons in justifying its actions despite their irrelevancy under the GATT rules. Perhaps, such defence could be explained by the fact that those cases were, in fact, handled by different Ministries, which often caused the problems of "communication" and "know-how sharing" among various Ministries.²² The problem basically arose from the "inter-rivalry" relationship among Ministries, which could be deemed to have influenced some of Japanese defeats experienced during the 80's.

In stark contrast to those cases, the *Parts and Components* case²³ ('88) in which Japan was a "Claimant" brought it its first legal victory. This case could be seen as an earliest signal which demonstrated appropriate and technical legal arguments being made tactically under the GATT system. One cannot deny that this positive, though unprecedented result for Japan must have given a great deal of confidence to its authorities for further reliance on the multilateral approach under GATT. In other words, they realised that the GATT system could work in favour of their national interests if they pursue more technical and legal arguments in accordance with the multilateral rules.

See generally, Appendix II to the thesis.

¹⁹Agriculture case, see **BISD 35S/163 (1989)**; also see Section 7.1.1.3. in Chapter 7 of the thesis.

²⁰Leather case, see **BISD 31S/94 (1985)**; also see Section 7.1.1.1. in Chapter 7 of the thesis.

²¹Alcohol-I, see **BISD 34S/83 (1988)**; also see Section 7.1.1.2. in Chapter 7 of the thesis.

²²Matsushita, Mitsuo., and Thomas J. Schoenbaum, Japanese International Trade and Investment, Tokyo University Press, 1989, pp. 24-25, reproduced in Jackson, J.H., William J. Davey and Alan O. Sykes, Jr., Legal Problems of International Economic Relations - cases, materials and text, Third Edition, West Publishing Co., St. Paul, MN, 1995, pp. 222-223.

²³Parts and Components case, see **BISD 37S/132 (1991)**; also see Section 7.1.2.1. in Chapter 7 of the thesis.

One should also mention another successful story for Japan, that is, the *SPF Dimension Lumber* case.²⁴ What is noteworthy in this particular case is that Japan won for the first time as a respondent. This result may have increased "trust" among Japanese authorities in the credibility of the GATT DS system. Furthermore, Japan also may have been reassured that its tactics towards leading trade disputes could result in a positive outcome under the multilateral system.

3) Japanese behaviour in the recent dispute on Auto and Auto parts between Japan and the United States²⁵ could be regarded as a clear illustration of Japan's new attitude towards its dispute. This dispute displayed a number of important aspects in terms of Japan's multilateral approach in resolving disputes in accordance with the GATT/WTO DS procedures. The dispute was eventually resolved "bilaterally" and an agreement was reached on 28 June 1995.²⁶ In fact, Japan persisted in taking a multilateral/rule-oriented approach throughout its talks with the U. S. In other words, Japan has insisted on a multilateralism as an approach against the U.S. threats of sanctions under Section 301, which was not the case before in the Japanese DS history.

Besides the findings from the case studies, the following also offer a significant circumstantial evidence to support the same line of argument pointed out above.

²⁴SPF Dimension Lumber case, see **BISD 36S/167 (1990)**; also see Section 7.1.2.2. in Chapter 7 of the thesis.

²⁵Articles on this dispute can be found in, *The Economist*, May 13th-19th 1995 at 18, 79-80; *ibid.*, May 20th-26th 1995 at 81; *ibid.*, June 17th-23th 1995 at 97; *ibid.*, June 24th-30th 1995 at 95; also in WTO, *WTO Focus*, (No. 3) May-June 1995; for criticisms on the U.S. trade policy [with respect to the two elements, i.e. (1) "aggressive unilateralism", (2) demands for managed trade in the form of "Voluntary Import Expansions (VIEs)"] over the car disputes, see Bhagwati, Jagdish., "The US-Japan car dispute: a monumental mistake", 72 *Int'l affairs* No. 2 (April 1996), pp. 261-279; also read in general Abels, Tracy M., "The World Trade Organisation's First Test: The United States - Japan Auto Dispute", 44 *UCLA L. Rev.*, Part. 2 (1996), pp. 467-526.

²⁶See, Section 8.1.1.1. in Chapter 8 of the thesis.

One aspect is human resources, i.e., the Japanese diplomats who have been involved in negotiations with trade partners. Unlike the previous generation of diplomats, Japan's new generation of bureaucrats are tougher and more eloquent at the negotiation table. For example, it was this new generation of diplomats that the U. S. negotiators had to face in the recent *Auto and Auto parts* dispute.²⁷ There are two characteristics shared in common by the new-type diplomats:

"(i) as they grew up after World War II, they are free from the mixed feelings of the previous generation as regards the occupation by the United States; and, (ii) they were agreed in resolving the prolonged dispute, and not to be 'pushed about' by the U. S. any more, and this, contrary to Washington's expectations, has indeed happened."²⁸

Thus, this factor could also encourage Japan, which now follows "multilateralism" in its dispute, to be more active in the use of the GATT/WTO DS system with less hesitation. Indeed, a new era is emerging in Japanese policy towards DS.

The other event to be noted here is that the Industrial Structure Council, an official advisory body to the MITI, has been publishing an annual report since 1992,²⁹ which lists the trade policies and measures, and violations of internationally agreed rules, of its trade partners, and clearly expresses its opinion that Japan would bring such illegal acts to the DS system of GATT/WTO if necessary. In these reports, the MITI explicitly supports a rule-oriented/multilateral approach for resolving disputes, and states that Japan would apply to the GATT/WTO DS system, if no progress could be seen concerning such alleged illegal acts conducted by Japan's trade partners.³⁰ This

²⁷The Financial Times, "Japan's new breed of diplomat, 26 June 1995 at 12.

²⁸A recent report cited the new generation's toughness exposed as a one of the factors in prolonging the dispute over cars between Japan and the U. S.; see *ibid.*, Congressional Research Service Report (No detail was given).

²⁹Industrial Structure Council (ed.), Report on Unfair Trade Policies, Research Institute of International Trade and Industry Publication Department, Tokyo, 1992, 93, 94; this report series was re-titled in 1995 as, 1995 Report on the WTO Consistency of Trade Policies by Major Trading Partners.

³⁰According to this report, there are three main target areas:

(i) identifying and analysing trade policies and measures taken by Japan's major trading partners nominated by Japan, such as the United States, the European Union, Korea, Hong Kong, Singapore, Thailand, Australia, Malaysia, Indonesia and Canada, based on internationally agreed rules; (ii) promoting free trade by seeking to bring a dispassionate and constructive approach to its discussion of trade relations and policies; and, (iii) highlighting

report may be regarded as a manifestation of Japan's policy on DS towards a multilateral approach.

Finally, to reiterate the obvious but important point that the WTO DS system will be successful only if the major world economies set an example for the rest, including the less developed countries which have been rather sceptical about the GATT DS system for many years. Now, it is time for Japan and other major economies to contribute to developing world trade under the multilateral trading system. As for Japan, as we have seen in this study, whenever dispute arises, it has already committed itself to observe the multilateral rules under the new WTO system.

the importance of using WTO DS procedures to resolve problematic trade policies and measures multilaterally.

In fact, in October 1992, Japan requested the establishment of a panel against the EC concerning antidumping duty imposing by the EC on imports of audio cassettes from Japan. As a result of discussions over the terms of reference between the parties, the panel (established on 30 October 1992) finally set out its work in February 1994. In 28 April 1995, the panel report (ADP/136) was circulated to the members of the Committee on Anti-Dumping Practices [the "Cttee"]. The Panel recommended that the Cttee request the EC to reconsider its anti-dumping determination in the light of its obligation under the Anti-Dumping Agreement [the "Agreement"]. The Panel also recommended that the Cttee request that the EC bring its Basic Regulation into conformity with its obligation stipulated in the Agreement. At the first regular meeting of the Cttee, held on 12 June 1995, the panel report was considered by the Cttee members. At this meeting, although Japan urged the adoption of the panel report, the EC requested extra time to examine it. In October 1995, the Cttee once again discussed the report, nonetheless, failed to adopt it; for a summary of this case, see GATT, GATT Activities 1992, Geneva, pp. 29-30, and also, *ibid.*, GATT Activities 1994-1995, pp. 55-57.

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APPENDIX I

THE STRUCTURE OF THE WTO AGREEMENT

MARRAKESH AGREEMENT ESTABLISHING THE WTO

ANNEX 1

ANNEX 1A: MULTILATERAL AGREEMENTS ON TRADE IN GOODS

General Agreement on Tariffs and Trade 1994

- Understanding on the Interpretation of Article II:1(b) of the General Agreement on Tariffs and Trade 1994
- Understanding on the Interpretation of Article XVII of the General Agreement on Tariffs and Trade 1994
- Understanding on Balance-of-Payments Provisions of the General Agreement on Tariffs and Trade 1994
- Understanding on the Interpretation of Article XXIV of the General Agreement on Tariffs and Trade 1994
- Understanding in Respect of Waivers of Obligations under the General Agreement on Tariffs and Trade 1994
- Understanding on the Interpretation of Article XVIII of the General Agreement on Tariffs and Trade 1994
- Marrakesh Protocol to the General Agreement on Tariffs and Trade 1994

Agreement on Agriculture

Agreement on the Application of Sanitary and Phytosanitary Measures

Agreement on Textiles and Clothing

Agreement on Technical Barriers to Trade

Agreement on Trade-Related Investment Measures

Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994

Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade 1994

Agreement on Preshipment Inspection

Agreement on Rules of Origin

Agreement on Import Licensing Procedures

Agreement on Subsidies and Countervailing Measures

Agreement on Safeguards

ANNEX 1B: General Agreement on Trade in Services

ANNEX 1C: Agreement on Trade-Related Aspects of Intellectual Property Rights

ANNEX 2: Understanding on Rules and Procedures Governing the Settlement of Disputes

ANNEX 3: Trade Policy Review Mechanism

ANNEX 4: Plurilateral Trade Agreements

- Agreement on Trade in Civil Aircraft
- Agreement on Government Procurement
- International Dairy Agreement*
- International Bovine Meat Agreement*

[* Those agreements were terminated from the Annex 4 at the end of 1997, see Press/78 (30 September 1997)]

APPENDIX II

THE TABLE OF GATT/WTO CASES/DISPUTES

(Cases in upper-case are not dealt with in the main text of the thesis;
active cases, as of 25 January 1999, are indicated with an asterisk)

	Japan's attitude: an "old" pattern (predominated until the late 80's; characterised as more bilateral, political, and power-oriented approach/settlement)	Japan's attitude: a "current" pattern (emerged around the late 80's; characterised as more multilateral, judicial, and rule-oriented approach/settlement)
Japan was involved in disputes as a "Complainant"	<p><u>No formal action was taken by the Government (i.e. an action would have been taken entirely at private sectors' own discretion)</u></p> <p>Cases/Disputes: N/A</p>	<p><u>Rule-oriented approach; a public accusation of contentious issues through reports¹</u></p> <p>Cases/Disputes: the <i>Semiconductor Retaliation</i> ('87); the <i>Parts and Components</i> ('88); the <i>Auto and Auto Parts</i> ('95); the <i>INDONESIA "NATIONAL CAR"</i> ('98); the U.S. <i>"MASSACHUSETTS BURMA LAW"</i>(WT/DS95)*; the <i>CANADA "AUTO"</i> (WT/DS139)*</p>
Japan was involved in disputes as a "Respondent"	<p><u>Less judicial (or more emotional) arguments</u></p> <p>Cases/Disputes: the <i>Leather</i> ('83); the <i>Alcohol-I</i> ('86); the <i>Agriculture</i> ('86); the <i>Semiconductor</i> ('87); the <i>Beef and Citrus</i> ('88)</p>	<p><u>More judicial (or technical) arguments</u></p> <p>Cases/Disputes: the <i>Alcohol-II</i> ('95); the <i>Film</i> ('96); the <i>JAPAN "APPLE"</i> (an appellate report due in Feb. '99)*; the <i>JAPAN "LEATHER-II"</i> (WT/DS147)* [cf. the <i>SPF</i> ('87) may be included in this group]</p>
<p>¹See, in general, an annual report published since 1992, entitled, <u>Report on Unfair Trade Policies by Major Trading Partners - Trade Policies and GATT Obligations</u> and re-titled as, <u>Report on the WTO Consistency of Trading Policies by Major Trading Partners</u>, since 1994, Industrial Structure Council, the MITI, Tokyo, Japan.</p>		

APPENDIX III

SUMMARIES OF THE RECENT CASES

The next two disputes have come to an end after the cut-off date (30 June 1998) of the case studies in Chapters 7 and 8 of the thesis. The aim of this appendix is to keep up with the new developments in the dispute settlement system of WTO. Furthermore, due to the restrictions of both time and the volume of words in this dissertation, I simply provide a summary of each case as an addendum of the case studies conducted in Chapters 7 and 8.

1. Indonesia - Certain Measures Affecting the Automobile Industry (WT/DS54, 55, 59 & 64/R) (2 July 1998) [On 23 July 1998, the DSB adopted the Panel Report and currently in implementation process]¹

Background:

Indonesia has had programmes to support the development of its automotive industry since 1960. The present dispute concerned three programmes maintained by Indonesia with respect to motor vehicles and parts and components, and those programmes were: (i) the 1993 Incentive System (which was amended in 1995 and 1996); (ii) the February 1996 National Car Programme (the "February 1996 Car Programme"); (iii) the June 1996 National Car Programme, i.e. an extension of the February 1996 Car Programme (the "June 1996 Car Programme").

(i) The 1993 Incentive System consisted of:

(a) import duty relief for parts and components of cars depending on meeting local content requirements for the finished products, where the amount of duties varies according to the percentage of local content (Decree 645/93 amended by 223/95); above a certain local content percentage, a full exemption from duties applies to imports of parts and components.

(b) reduction from sales tax on goods (the "sales tax") on certain categories of motor vehicles (below 1600cc), depending on them being manufactured locally and in some cases depending on a minimum local content requirement of 60% (Decree 645/93 as amended in 1996 by Regulation 36).

(ii) The 1996 National Car Programme consisted of two main sets of measures (Decree 31/96):

¹On 8 October 1988, the EC requested that the "reasonable period of time" for implementation of recommendations and rulings of the DSB regarding the 1993 Programme be determined by binding arbitration pursuant to Article 21:3(c) of the DSU. Mr. Christopher Beeby (arbitrator) determined that the reasonable period of time for Indonesia to implement the recommendations and rulings of the DSB in this case is twelve months from 23 July 1998 (i.e. the date of adoption of the Panel Report by the DSB); WT/DS54/15, WT/DS55/14, WT/DS59/13, WT/DS64/12 (7 December 1998).

(a) The first set of measures (Presidential Decree 42/96), the February 1996 Car Programme, provided for the grant of "pioneer" or National Car company status to Indonesian car companies that meets specified criteria as to ownership of facilities, use of trademarks, and technology.

Maintenance of the pioneer status was depend on the National Cars' meeting increasing local content requirements over a three year period (i.e. 20% at the end of the 1st year; 40 % at the end of the 2nd year; 60% at the end of the 3rd year).

The benefits provided were: (1) exemption form luxury tax on sales of National Cars; and (2) exemption from import duties on parts and components.

(b) The second set of measures (Presidential Decree 42/96 and Ministerial Decree 142/96), the June 1996 Car Programme, provided that National Cars manufactured in a foreign country by Indonesian nationals and which fulfil the local content requirements prescribed by the Ministry of Industry and Trade, shall be treated the same as National Cars manufactured in Indonesia, i.e. exempt from import duties and luxury tax. In accordance with Decree 142/96, imported National Cars are deemed to comply with the 20% local content requirement for the end of first production year if the overseas producer manufacturing the National Cars "counter-purchases" Indonesian parts and components that account for at least 25% of the C&F value of the imported cars.

In fact, there was only one "National Car" company, PT TPN, which was granted pioneer status only a few days after the adoption of the National Car programme on 19 February 1996. In June 1996, PT TPN was authorised to import duty free under the June Extension of the National Car Programme (i.e. the June 1996 Car Programme) 45,000 units of the model Timor S515.

On 25 February 1998, Indonesia notified the Subsidies Committee that, as of 21 January 1998, it had terminated all subsidies previously granted under the National Car programme. On 2 March 1998, Indonesia notified the Panel and requested the Panel to terminate the dispute settlement proceedings, at least it relates to the 1996 National Car programme measures.

(Notifications by Indonesia to WTO Committees)

On 23 May 1995, Indonesia made a notification with respect to the 1993 Incentive System to the TRIMs Committee under Article 5.1 of the TRIMs Agreement.² On 28 October 1996, Indonesia notified the TRIMs Committee that it was "withdrawing" its notification related to automobiles because it considered that its programme was not a TRIM;³ on the same day Indonesia made a notification with respect to its 1993 Incentive System and its 1996 National Car programme to the SCM Committee.⁴

²G/TRIMS/N/1/IND/1.

³G/TRIMS/N/1/IND/1/Add.1.

⁴C/SCM/N/16/IDN.

(Claims of the Complainants)

The complainants were Japan, the EC and the U.S., who challenged against the Indonesia's car programme. Although a similar argument was made as a main focus of their claim, there were some differences among them. The complainants made a claim on: i) Local-content requirements; ii) Tax discrimination; iii) MFN discrimination; iv) Absence of notification and partial administration; v) Serious prejudice; vi) Extension of the scope of existing subsidies; vii) National treatment violation with respect to the acquisition and maintenance of trademarks, and the use of trademarks; viii) Introduction of special requirements in respect of the use of trademarks.

(Indonesia's General Defence)

The Indonesia's general defence to the above claims was that the SCM Agreement was *lex specialis* to this dispute. For Indonesia, this principle meant that because the measures at issue were subsidies, they were governed by exclusively by Article XVI of GATT and the SCM Agreement. The Indonesia's argument was to be two-fold:

(i) The only law applicable to this dispute is the SCM Agreement:

1. There is a general conflict between Article III of GATT and the SCM Agreement. (Indonesia in its second submission expanded this argument to include claims under Article I of GATT as well);
2. The application to this dispute of Article III of GATT would reduce the SCM Agreement to "inutility";
3. General rules of treaty interpretation require rethinking the scope of Article III:8(b);
4. Since Article III is not applicable, the TRIMs Agreement is not applicable.

(ii) Should Article III and/or the TRIMs Agreement be considered to apply to this dispute?; There are specific conflicts between some of the provisions of the SCM Agreement, on one hand, and some provisions of Article III on which the complainants base their claims, on the other hand; For Indonesia, any and all conflicts should be resolved in favour of the SCM Agreement (which permits the car programmes under examination according to Indonesia).

Findings and Conclusions:

(Preliminary Objections with respect to 4 issues)

i) Presence of private lawyers (i.e. the U.S. request to exclude from meetings of the Panel two private lawyer in the Indonesian delegation):

On 3 December 1997, at the first meeting of the parties, the Panel ruled that it was for the Indonesian government to nominate the members of its delegation to meeting of this Panel.⁵ The Panel insisted that all members

⁵Cf. The Banana case contained a specific provision requiring the presence only of government officials, see the Appellate and Panel Reports on EC- Regime for the Importation, Sale and Distribution of Bananas, WT/DS27, adopted on 25 September 1997.

of parties' delegations to respect the provision of the DSU and the confidentiality of the proceedings.

ii) The alleged loan to PT TPN as a measure covered by the terms of reference of this panel:

Indonesia raised a preliminary objection, at the first meeting of the Panel with the parties, to the U.S.' claim with respect to a \$US 690 million loan to PT TPN, on the basis that this loan was not within the Panel's terms of reference. The Panel ruled that the loan was not *identified as a specific measure* in that document as required by Article 6.2 of the DSU. Furthermore, the U.S. indeed stated that the loan was not identified in the U.S. request, because it had not yet been made. For the Panel, the U.S. in its request for panel had clearly identified the measures to be considered by the Panel, and those measures did not include this loan. Accordingly, the Panel concluded that the loan in question was not within the terms of reference of this Panel.

iii) Business proprietary information:

With respect to three points in its first submission, the U.S. indicated that it had further information relevant to its serious prejudice claims but that this information was "business proprietary" and that the U.S. was reluctant to provide it to the panel in the absence of "adequate procedures" to protect such information.

At the first meeting, the Panel ruled that it encouraged all parties to submit relevant data to the Panel as early as possible. The Panel, however, noted that it was a matter for each party to decide when and if to submit information and argumentation within the schedule set forth by the Panel. The Panel also stated that if any party considered that it had not had an adequate opportunity to address any such new data and argumentation, the Panel would take all reasonable steps to insure that all parties have had a full opportunity to respond to the factual information and argumentation submitted to the Panel. Despite the invitation by the Panel, the U.S. did not propose or request the Panel to adopt any such procedure.

iv) Whether the National Car programme has expired and should therefore not be examined by this panel:

On 25 February 1998, Indonesia notified the Chairman of the Subsidies Committee by letter that, as of 21 January 1998, it had terminated all subsidies previously granted under the National Car programme. (On 2 March 1998, Indonesia notified the Panel and requested the Panel to terminate the dispute settlement proceeding, at least as it relates to the 1996 National Car programme measures.) Indonesia, therefore, considered the Presidential Instruction establishing the National Car programme as to be "obsolete". In fact, this communication from Indonesia reached to the Panel after the deadline of 30 January 1998 set

by the Panel for the submission of information and arguments in this case.

The Panel considered that it was appropriate for it to make findings in respect of the National Car Programme. In this respect, the Panel noted that in the previous GATT/WTO cases, in which a measure included in the terms of reference was otherwise terminated or amended after the commencement of the panel proceedings, panels have nonetheless made findings in respect of such a measure.⁶

(Main Conclusions)

With respect to the Indonesia's argument that there was a general conflict between Article III and the SCM Agreement (and Article XVI) and that the Indonesian car programmes were governed exclusively by the SCM Agreement, the Panel noted that Article III and Article XVI have co-existed since the inception of the GATT system of rules. As to Article III of GATT and the SCM Agreement, the Panel considered that Article III and the SCM Agreement have, in general, different coverage and do not impose the same type of obligations. The Panel further rejected the Indonesia's argument that the application of Article III of GATT to subsidies would reduce the SCM Agreement to "inutility". With respect to Indonesia's argument that its measures are only governed by the SCM Agreement, the Panel responded that Article III:8(b) confirms that the obligations of Article III and those of Article XVI (and the SCM Agreement) are different and complementary: subsidies to producers are subject to the national treatment provisions of Article III when they discriminate between imported and domestic products.

The Panel rejected Indonesia's general defence that the only applicable law to this is the SCM Agreement, and concluded that the obligations contained in the WTO Agreement are generally cumulative and can be complied with simultaneously and that different aspect and sometimes the same aspects of a legislative act can be subject to various provisions of the WTO Agreement.

As to the Indonesia's argument that since Article III was not applicable, the TRIMs Agreement which did not add anything to Article III was not applicable to this dispute, the Panel stated that Article III was, in general, applicable and further that the TRIMs Agreement was legally distinct from Article III. Accordingly, even if Article III were not applicable as the Indonesia's view, the TRIMs Agreement remained applicable.

The Panel concluded:

(a) that the local content requirements of the 1993 and of the February 1996 car programmes to which are linked (i) sales tax benefits on finished motor vehicles incorporating a certain percentage value of domestic products or on National Cars

⁶See, for example, the report of Appellate Body on Argentina -Certain Measures Affecting Imports of Footwear, Textiles, Apparel and Other Items, WT/DS/56/AB/R (27 March 1998).

and (ii) customs duty benefits for imported parts and components used in finished motor vehicles incorporating a certain percentage value of domestic products or used National Cars violate the provisions of Article 2 of the TRIMs Agreement;

(b) that the sales tax discrimination aspects of the 1993 and the February and June 1996 car programmes in favour of domestic motor vehicles incorporating a certain percentage value of domestic products and National Car violated the provisions of Article III:2 of GATT;

(c) that the customs duty and sales tax benefits of the June 1996 car programme in favour of imported National Cars and the customs duty benefits of February 1996 car programme in favour of imported parts and components to be used in National Cars assembled in Indonesia violate Article I of GATT;

(d) that the European Communities have demonstrated by positive evidence that Indonesia has caused, through the use of specific subsidies provided pursuant to the National Car programme, serious prejudice to the interests of the European Communities within the meaning of Article 5(c) of the SCM Agreement;

(e) that the United States has not demonstrated by positive evidence that Indonesia has caused, through the use of specific subsidies provided pursuant to the National Car programme, serious prejudice to the interests of the United States within the meaning of Article 5(c) of the SCM Agreement;

(f) that Indonesia has not violated Article 28.2 of the SCM Agreement;

(g) that the United States has not demonstrated that Indonesia is in breach of its obligations under Article 3 of the TRIPS Agreement in respect of the acquisition of trademark rights or the maintenance of trademark rights or in respect of the use of trademarks specifically addressed in Article 20 of the TRIPS Agreement nor has it demonstrated that measures have been taken that reduce the degree of consistency with the provisions of Article 20 and which would therefore be in violation of Indonesia's obligations under Article 65.5 of the TRIPS Agreement.

2. Japan - Measures Affecting Agricultural Products (WT/DS76/R) (27 October 1998) [The report of the Panel was circulated to Members on 27 October 1998]⁷

Background:

Despite the U.S. efforts to export various fruit products to Japan since the early 1970's, the size of exports of those products to Japan represent only a small part in

⁷The Financial Times, "Japan to appeal over apples", 29 October 1998 at 6. According to this article, the MAFF (Ministry of Agriculture, Forestry, and Fisheries) of the Japanese government said that it would appeal against the panel ruling; the Notification of an Appeal by Japan, WT/DS76/5 (24 November 1998); the report of the Appellate Body will be out at the end of February 1999.

comparison to that of U.S. exports to world-wide, which was caused by Japan's troublesome and time-consuming varietal testing requirement. In fact, in some cases, the U.S. filed varieties application of a product over a decade ago.

Facts and Procedure:

Japan's prohibition, under quarantine measures, of imports of agricultural products was the main issue in the present dispute. According to the measures, Japan prohibited the importation of U.S. agricultural products on which Japan claimed the pest codling moth might occur. Japan therefore required, under the measures, quarantine treatment until the quarantine treatment has been tested for each varieties, even if the proposed treatment has proved to be effective for other varieties of the same product category. The products at issue included apples, nectarines, cherries and walnuts. There were a number of different varieties within each of the product categories. Such varieties could be noticed, for instance, in colour, ripening time, taste or other characteristics. To obtain approval to import additional varieties of a product through such a test could take up to 4 years. While, in the U.S. view, it would be sufficient to test the treatment on one variety within each product category in order to prove that the treatment would be effective for the rest of varieties within that category. The U.S. alleged that Japan's measures at issue were introduced in order to protect its own agricultural products for that pest, which in fact did not occur in Japan.

(Consultation with experts)

The Panel recalled that Article 11:2 of the SPS Agreement provided that, for a dispute under this Agreement involving scientific or technical issues, a panel should seek advice for experts chosen by the panel in consultation with the parties to the dispute. In this panel, the Panel selected three experts in the area of entomology and pesticide fumigation and sought a scientific and technical advice individually subject to a number of questions (the Panel submitted initially 18 questions and a few additional ones). In the final report, the Panel referred to the advice submitted by those experts in support of a number of its legal findings.

Findings and Conclusions:

The Panel considered that the main issue in dispute was the Japan's requirement that the exporting countries need to demonstrate the efficacy of their quarantine treatment in order to obtain access to the Japanese market for each variety of a given product (the "Japan's varietal testing requirement").

To begin with, the Panel examined whether there was sufficient scientific evidence in support of the varietal testing requirement maintained by Japan (Article 2.2 of the SPS Agreement). With respect to four out of eight products at issue (i.e. apples, cherries, nectarines and walnuts), the Panel found Japan maintained the varietal testing requirement without scientific evidence. The Panel further reached the conclusion that the varietal testing requirement could not be considered as a provisional measure in cases where scientific evidence is insufficient, since Japan did not seek to obtain the additional information necessary for a more objective

assessment of risk and review the measure accordingly within a reasonable period of time (Article 5.7 of the SPS Agreement).

The Panel also found that there was alternative measures which would also satisfy the level of sanitary and phytosanitary protection expected by Japan and which would be less trade-restrictive than the current level required by Japan. The Panel particularly examined certain alternatives proposed by the experts. The current Japan's requirement was found to be more trade-restrictive than required to achieve appropriate level of protection, taking into account technical and economic feasibility (Article 5.6 of the SPS Agreement). Nonetheless, the Panel was not convinced that there was sufficient evidence to decide that "testing by product" (proposed by the U.S) would fulfil the appropriate level of protection expected by Japan.

The Panel found that Japan, by not having published the varietal testing requirement with respect to any of the products at issue, had acted inconsistently with its transparency obligations under paragraph 1 of Annex B of the SPS Agreement.

Finally, the Panel concluded that Japan, by maintaining the varietal testing requirement, had acted inconsistently with Article 2.2, 5.6 and 7 of the SPS Agreement.

APPENDIX IV

THE LIST OF JAPANESE DISPUTES UNDER GATT/WTO

- GATT DISPUTES -

[Japan as "complainants"]

1. United States - Suspension of customs liquidation ("Zenith case") (BISD 24S/135)
2. EEC - Import restrictive measures on video tape recorder ("Poitiers case")
3. United States - Restrictions on certain Japanese products ("Semiconductor Retaliation case")
4. EEC - Regulation on imports of parts and components (BISD 37S/132)
5. EEC - Regulation on imports of parts and components (Anti-dumping Code)
6. EC - Anti-dumping duties on audio tapes in cassettes originating in Japan (ADP/136)
7. EEC - Refund of anti-dumping duties (ADP/78)
8. United States - Provisional anti-dumping measures against imports of certain steel flat products (ADP/100)

[Japan as "respondents"]

1. 15 Developed Countries (including Japan) - Uruguayan recourse to Article XXIII (Uruguay) (BISD 11S/95; BISD 13S/35)
2. Japan - Restrictions on imports of beef and veal (Australia) (BISD 26S/81)
3. Japan - Measures on imports of thrown silk yarn (United States) (BISD 25S/107)
4. Japanese measures on imports of leather (United States)
5. Japan - Restraints on import of manufactured tobacco from the United States (United States) (BISD 28S/100)
6. Japan's measures on imports of leather (Canada) (BISD 27S/118)

7. Japan - Certification procedures for metal softball bats (United States)
8. Japan - Nullification and impairment of benefits and impediment to the attainment of GATT objectives (EEC)
9. Panel on Japanese measures on imports of leather (United States) (complained on 5/1/83) (BISD 31S/94)
10. Japan - Single tendering procedures (United States)
11. Japan - Quantitative restrictions on imports of leather footwear (United States)
12. Japan - Customs duties, taxes and labelling practices on imported wines and alcoholic beverages (EEC) (BISD 34S/83)
13. Japan - Restrictions on imports of certain agricultural products (United States) (BISD 35S/163)
14. Japan - Restrictions on imports of herring, pollock and surimi (United States)
15. Japan - Trade in semiconductors (EEC) (BISD 35S/116)
16. Japan - Copper trading practices in Japan (EEC) (BISD 36S/199)
17. Canada/Japan: Tariff on imports of spruce, pine, fir, (SPF) dimension lumber (Canada) (BISD 36S/167)
18. Japan - Import restrictions on beef (New Zealand)
19. Japan - Restrictions on imports of beef and citrus products (United States)
20. Japan - Restrictions of beef (Australia)
21. Japan - Restrictions on imports of certain agricultural products [follow-up] (Australia, New Zealand, United States) (DS25)
22. Japan - Measures affecting imports of certain telecommunication equipment (EEC) (DS52)

- WTO DISPUTES -

[Japan as a "complainants"]

1. United States - Imposition of import duties on automobiles from Japan under Sections 301 and 304 of the Trade Act of 1974 (WT/DS6/...)
2. Brazil - Certain automotive investment measures (Japan) (WT/DS51/...)
3. Indonesia - Certain measures affecting the automobile industry (1) (Japan) (WT/DS55/R)
4. Indonesia - Certain measures affecting the automobile industry (2) (Japan) (WT/DS64/R)
5. United States - Measure affecting government procurement (Japan) (WT/DS95/...)
6. Canada - Certain measures affecting the automotive industry (WT/DS139/...)

[Japan as "respondents"]

1. Japan - Taxes on alcoholic beverages (EC) (WT/DS8/R; WT/DS8/AB/R)
2. Japan - Taxes on alcoholic beverages (Canada) (WT/DS10/R; WT/DS10/AB/R)
3. Japan - Taxes on alcoholic beverages (United States) (WT/DS11/R; WT/DS11/AB/R)
4. Japan - Measures affecting the purchase of telecommunications equipment (EC) (WT/DS15/...)
5. Japan - Measures concerning sound recordings (United States) (WT/DS28/...)
6. Japan - Measures concerning sound recordings (EC) (WT/DS42/...)
7. Japan - Measures affecting consumer photographic film and paper (United States) (WT/DS44/R)
8. Japan - Measures affecting distribution services (United States) (WT/DS45/...)
9. Japan - Measures affecting imports of pork (EC) (WT/DS66/...)

10. Japan - Procurement of a navigation satellite (EC) (WT/DS73/...)

11. Japan - Measures affecting agricultural products (United States)
(WT/DS76/R)

12. Japan - Tariff quotas and subsidies affecting leather (EC) (WT/DS147/...)