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David Palmeter and Petros C. Mavroidis

Excerpt

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# 1

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## Overview

### § 1.01 The ITO, the GATT, and the WTO

#### [1] *Bretton Woods and the Havana Charter*

Even as World War II was being fought, allied leaders began to plan for the post-war world which, they hoped, would not be characterized by the economic isolationism that had marked the pre-war years. Many believed that this contributed in no small way to the deepening of the Great Depression and the onset of war. In a 1941 speech entitled “Post-War Commercial Policy,” United States Undersecretary of State Sumner Wells said:

Nations have more often than not undertaken economic discriminations and raised up trade barriers with complete disregard for the damaging effects on the trade and livelihood of other peoples, and ironically enough, with similar disregard for the harmful resultant effects upon their own export trade.

The resultant misery, bewilderment, and resentment, together with other equally pernicious contributing causes, paved the way for the rise of those very dictatorships which have plunged almost the entire world into war.<sup>1</sup>

These economic concerns eventually led to the famed July 1944 conference at Bretton Woods, New Hampshire, and the resulting “Bretton Woods organizations,” the International Bank for Reconstruction and Development (commonly known as the World Bank) and the International Monetary Fund. Probably because Bretton Woods was attended only by representatives of finance ministries and not by representatives of trade ministries, an agreement covering trade was not negotiated there. A

<sup>1</sup> US Dep’t. of State, Pub. No. 1660, Commercial Policy Series 71 (1941), *quoted* in John H. Jackson, *WORLD TRADE AND THE LAW OF GATT* 38 (Bobbs-Merrill, 1969).

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trade agreement was very much in the minds of allied economic leaders, however, and in early December 1945, the United States issued a proposal for an International Trade Organization, the ITO. But it was not the time for such an ambitious proposal. To the contrary, almost five years later to the day, on December 6, 1950, the United States Department of State announced that the ITO was dead, killed by the United States Congress, which – eerily reminiscent of the United States Senate’s treatment of the Treaty of Versailles and the League of Nations – refused to approve it.<sup>2</sup> Still, all was not lost. An odd portion of the ITO, in an odd way, survived. It was known as the General Agreement on Tariffs and Trade, or GATT, and it lasted for nearly half a century, for 47 years. On January 1, 1995, it was replaced by the World Trade Organization, the WTO, an entity broader both in its reach and in its effectiveness, but which is not at all what the ITO was intended to be.

[2] *The negotiation of GATT*

The ITO was ambitious, certainly too ambitious for the United States Congress and perhaps, with the advantage of hindsight, too ambitious by almost any reasonable standard. It was negotiated over a two-year period, from 1946 through 1948, at a series of meetings in London, New York, Geneva, and finally at a United Nations Conference on Trade and Employment in Havana, which produced the “Havana Charter for an International Trade Organization.” As the conference name suggests, the ITO encompassed not only trade policy, but also employment policy. In addition, it covered commodity agreements, economic development, and restrictive business practices.

While the more ambitious provisions of the ITO were being negotiated, however, governments were interested in relaxing tariffs and other trade restrictions more rapidly. A Drafting Committee, under the sponsorship of the Preparatory Committee charged with drafting the ITO charter,

<sup>2</sup> This section draws heavily on Richard N. Gardner, *STERLING-DOLLAR DIPLOMACY IN CURRENT PERSPECTIVE: THE ORIGINS AND PROSPECTS OF OUR INTERNATIONAL ECONOMIC ORDER* (Columbia Univ. Press ed., 1980); Robert E. Hudec, *THE GATT LEGAL SYSTEM AND WORLD TRADE DIPLOMACY* (2d ed., Butterworth, 1990); Jackson, *supra* note 1; and on the *WORLD TRADE ORGANIZATION, ANALYTICAL INDEX, GUIDE TO GATT LAW AND PRACTICE* (1995). In addition, John Jackson, *THE WORLD TRADING SYSTEM* (2d ed., MIT Press, 1997) provides an excellent history and description of the world trading system.

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meeting in January and February 1947 at Lake Success, New York, produced a full draft of the GATT. From April through October 1947, the members of the Preparatory Committee conducted a round of tariff negotiations in the course of their ITO work at the European Office of the United Nations in Geneva. This became the first of GATT's eventual eight rounds of negotiations. It produced the "Geneva Final Act," consisting of the Lake Success text of GATT and the schedules of tariff commitments made by the 25 governments taking part.<sup>3</sup> It also included a "Protocol of Provisional Application" or "PPA," a measure intended to be a temporary expedient, but which ended up being fundamental to GATT for its 47-year existence.

[3] *The Protocol of Provisional Application (PPA)*

The broad scope of the ITO called for changes in the laws of many signatory governments and, consequently, eventual legislative approval under their various constitutional systems before it could become effective. Some governments did not want to wait until that process was completed and, accordingly, at the end of October 1947, eight of them agreed to apply GATT provisionally as of January 1, 1948.<sup>4</sup> Under the terms of the PPA, the eight undertook to apply Parts I and III of GATT fully, and to apply Part II only "to the fullest extent not inconsistent with existing legislation."<sup>5</sup> Part I contained just two articles, dealing with non-discrimination among competing foreign suppliers (most-favored-nation, or MFN) and the schedule of tariff rates just negotiated. Part III contained articles dealing, for the most part, with administrative matters. The substantive heart of GATT, Part II, consisted of Articles III through XXIII. These included provisions covering national treatment; antidumping and countervailing duties; valuation of imports for customs purposes; marks of origin; import and export quotas and limitations; restrictions on imports for balance of payments purposes; exchange arrangements; subsidies; state trading enterprises; governmental assistance to economic development; emergency action on imports of particular products; exceptions to GATT

<sup>3</sup> FINAL ACT ADOPTED AT THE CONCLUSION OF THE SECOND SESSION OF THE PREPARATORY COMMITTEE OF THE UNITED NATIONS CONFERENCE ON TRADE AND EMPLOYMENT, UN Sales No. 1947.II/10; 55 UNTS 187 (1947).

<sup>4</sup> The eight were: Australia, Belgium, Canada, France, Luxembourg, the Netherlands, the United Kingdom, and the United States.

<sup>5</sup> 55 UNTS 308, 1 (a) and (b) (1947).

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obligations, including exceptions necessary to protect human, plant, and animal life, health, and safety; and exceptions for national security purposes. Part II thus provides the necessary market access complement to Part I.

Together, Parts I and II set out the basic policy agreed to in GATT for trade liberalization. It is a policy that is based on: (i) preference for tariff protection to other forms of protection, such as quantitative restrictions or quotas; (ii) following on this, abolition (in principle, but not always in practice) of all quotas; (iii) application of quotas only exceptionally and only with multilateral permission; (iv) most-favored-nation (MFN) treatment, granted in principle to all GATT parties, subject to specific, narrowly-drawn exceptions; and (v) national treatment granted to all products of GATT parties that have lawfully cleared customs.

The application of Part II only to the extent that its articles were consistent with existing legislation created what became known as the “grandfather rights.”<sup>6</sup> Consequently, parties with these grandfather rights were allowed to continue applying GATT-inconsistent measures notwithstanding their obligations under the General Agreement. Article XXIX:2 of GATT shows how temporary this was intended to be. It provides, “Part II of this Agreement shall be suspended on the day on which the Havana Charter comes into force.” This was expected to occur within a fairly short time, so that inconsistent domestic legislation was not expected to be long-lived. But because the Havana Charter never came into force, GATT, for its entire 47 years, was applied on a “provisional” basis.

## [4] GATT’s 47 “provisional” years

Between the October 1947 issuance of the Protocol of Provisional Application and its effectiveness on January 1, 1948, most of the other countries participating in the Geneva tariff negotiations also agreed to apply the Protocol. The 1947 Geneva negotiations were followed by seven additional negotiations, called “rounds,” each of which involved more participants as additional countries acceded to the General Agreement and the current Doha Development Round under the WTO:

<sup>6</sup> An example would be the US countervailing duty law, which did not require a determination of material injury, as called for by Article VI in Part II of GATT, until the United States agreed to include such a requirement for signatories to the so-called 1979 Tokyo Round Subsidies Code or for other countries that entered into comparable bilateral agreements with the United States.

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<i>Round</i> <sup>7</sup>	<i>Dates</i>	<i>Number of Parties</i> <sup>8</sup>
Geneva	1947	19
Annecy	1949	27
Torquay	1950	33
Geneva	1956	36
Dillon	1960–61	43
Kennedy	1962–67	74
Tokyo	1973–79	85
Uruguay	1986–94	128
Doha	2001–	146

All of the rounds through the 1960–61 Dillon Round dealt with tariff cuts. In the Kennedy Round, a first, relatively unsuccessful attempt was made to deal with so-called “non-tariff barriers,” or NTBs. As tariffs were progressively cut, NTBs became more prominent as trade barriers. A Kennedy Round Antidumping Code and an agreement dealing with a highly protectionist US method of valuing certain chemicals and footwear for customs purposes were not accepted by the US Congress on the stated grounds that in reaching these agreements, the US negotiators had exceeded their mandate.<sup>9</sup>

This experience soured many trading partners of the United States, who found themselves having to negotiate twice: first with the US negotiators and then with the Congress. If NTBs were to be dealt with in future negotiations, another way had to be found. Another way was found that took into account the need of US trading partners to know that a package put together with US negotiators would not be taken apart by the Congress, and the constitutional need of the United States to refer to Congress all

<sup>7</sup> The first four rounds are named for the place where they were held: Geneva; Annecy, France; and Torquay, England. The Dillon Round and the Kennedy Round were named after the United States Under Secretary of State, C. Douglas Dillon, and President John F. Kennedy, respectively, who were instrumental in starting the rounds. The Tokyo and Uruguay Rounds were named after the city and the country, respectively, where trade ministers agreed to launch the rounds, as was the Doha Development Round.

<sup>8</sup> Computations of the total number of parties vary from source to source, because some of the original 1947 group subsequently withdrew from GATT (e.g., China, Czechoslovakia) and because countries that acceded to GATT during the course of a round would be counted at the end, but not at the beginning. Counts of participants in GATT activities may vary too depending on how the European Union is accounted for – as a single entity or as individual Members.

<sup>9</sup> See Russell Long, *United States Law and the International Antidumping Code*, 3 INT’L LAWYER 464 (1969).

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agreements requiring statutory change, which was the case with most measures dealing with NTBs. The solution was the so-called “fast-track procedure” first included in the Trade Act of 1974.<sup>10</sup> Under this procedure, the Congress agreed that a bill implementing a negotiated agreement would not be amendable on the floor of either House of Congress, would not be stalled in Committee, and would receive a straight “yes or no” vote within a stated time period.

This provision permitted the Tokyo Round negotiations to go forward, and led to the adoption of a wide variety of side-agreements or “codes” dealing with non-tariff issues:

1. Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade (Antidumping Code)
2. Agreement on Interpretation and Application of Articles VI, XVI and XXIII of the General Agreement on Tariffs and Trade (Subsidies Code)
3. Agreement on Import Licensing Procedures
4. Agreement on Trade in Civil Aircraft
5. Agreement on Technical Barriers to Trade
6. Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade and Protocol to the Agreement (Customs Valuation Code)
7. Agreement on Government Procurement

The Tokyo Round negotiations were the most extensive ever undertaken, but the 1986–1994 Uruguay Round was even more extensive in both its reach and its results. Before turning to a discussion of the Uruguay Round, however, we shall review briefly the evolution of dispute settlement under GATT, particularly as it evolved after the Tokyo Round. As we shall see, dispute settlement was one of the major goals of the Uruguay Round negotiators, and one of their major accomplishments.

*[5] GATT dispute settlement<sup>11</sup>*

Early dispute settlement in GATT reflected its diplomatic roots. In fact, the process initially was referred to as “conciliation,” not as dispute

<sup>10</sup> Pub. Law 93-618, 88 Stat. 1978.

<sup>11</sup> This section draws heavily on Robert E. Hudec’s outstanding two-volume history of GATT dispute settlement, *THE GATT LEGAL SYSTEM AND WORLD TRADE DIPLOMACY*, *supra* note 2, and *ENFORCING INTERNATIONAL TRADE LAW: THE EVOLUTION OF THE MODERN GATT LEGAL SYSTEM* (Butterworth, 1993) (hereafter *ENFORCING INTERNATIONAL TRADE LAW*).

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settlement. It all began with a complaint in the summer of 1948 by the Netherlands against Cuba which presented the question: Does the most-favored-nation obligation of Article I apply to consular taxes? The matter was referred to the chairman, who ruled that Article I did apply. From these early beginnings of rulings by the chairman, disputes later came to be referred to working parties, consisting of the complaining party, the party complained against, and any others that had an interest. Eventually, the parties directly involved were dropped, and a three- or five-member panel process was adopted, using neutral panelists rather than representatives of parties with an interest in the issue. The term “panel” came from the term “panel of experts” – a term, Robert E. Hudec has noted, that was “coined long before GATT to describe an *ad hoc* group of government experts (rather than policy officials) convened to render an expert opinion about some technical question that is capable of being answered objectively. The term thus connoted objective decisions based on expertise rather than political representation of one’s government.”<sup>12</sup> Most of the advocates before panels and most of the panelists themselves – the “judges” – were diplomats, not lawyers. Not surprisingly, therefore, “legal rulings were drafted with an elusive diplomatic vagueness.”<sup>13</sup> The goal of the process was more to reach a solution mutually agreeable to the parties than to render a decision in a legal dispute.<sup>14</sup>

GATT dispute settlement was characterized as well by the fact that its procedural rules were very limited, largely because it was anticipated that the ITO rules soon would apply. The ITO Charter contained detailed dispute settlement rules that included a provision for the reference of questions to the International Court of Justice, the ICJ. The only dispute settlement rules in GATT, based on two of the proposed ITO rules, were GATT Articles XXII and XXIII, dealing, respectively, with consultations and with “nullification and impairment,” a phrase that was basic to the jurisprudence of GATT and now is basic to the jurisprudence of the WTO.

By themselves, the consultation provisions of Article XXII have no direct consequences. Article XXII:1 simply requires each contracting party to afford other parties adequate opportunity for consultation with respect to any matter affecting the operation of the Agreement. Article XXII:2

<sup>12</sup> Robert E. Hudec, *The Role of the GATT Secretariat in the Evolution of the WTO Dispute Settlement Procedure*, in Bhagwati & Hirsch (Eds), *THE URUGUAY ROUND AND BEYOND: ESSAYS IN HONOUR OF ARTHUR DUNKEL* (Springer, 1998).

<sup>13</sup> Hudec, *ENFORCING INTERNATIONAL TRADE LAW*, *supra* note 11, at 12.

<sup>14</sup> See, William J. Davey, *Dispute Settlement in GATT*, 11 *FORDHAM INTERNATIONAL LAW JOURNAL* 51, 65 (1987).

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authorizes the CONTRACTING PARTIES acting jointly, at the request of a contracting party, to consult with other parties on matters which were not resolved through Article XXII:1 consultations.<sup>15</sup> Eventually, these consultations became a basis for the generation of GATT's dispute settlement process, which was grounded in Article XXIII.

Article XXIII:1 provided that if any contracting party considered that any benefit directly or indirectly accruing to it under the Agreement was being nullified or impaired by another party, it could make written representations or proposals to that other party. If this did not lead to a satisfactory adjustment, the complaining party was authorized by Article XXIII:2 to refer the matter to the CONTRACTING PARTIES, who were required to investigate and make recommendations. In an appropriate case, Article XXIII:2 permitted the CONTRACTING PARTIES to authorize the complaining party to suspend the application of tariff concessions or other GATT obligations to the party found to be acting inconsistently with its obligations under the Agreement.

Neither article contained any specific procedures.<sup>16</sup> These evolved over time. Some formality was added at the conclusion of the Tokyo Round with the adoption of the *Understanding on Notification, Consultation, Dispute Settlement and Surveillance of 28 November 1979*, which included an annex setting out an *Agreed Description of the Customary Practice of the GATT in the Field of Dispute Settlement*. This *Description* noted, in part, that:

Panels set up their own working procedures. The practice for the panels has been to hold two or three formal meetings with the parties concerned. The panel invited the parties to present their views either in writing and/or orally in the presence of each other. The panel can question both parties on any matter which it considers relevant to the dispute. Panels have also heard the views of any contracting party having a substantial interest in the matter, which is not directly party to the dispute, but which has expressed in the Council a desire to present its views. Written memoranda submitted to the panel have been considered confidential, but are made available to the parties to the dispute. Panels often consult with and seek information from

<sup>15</sup> The term CONTRACTING PARTIES in upper case letters was the GATT convention for referring to joint action by all of the parties to the Agreement. Since GATT was an agreement, not an organization, GATT itself could not act. In lower case, the term referred to individual signatories.

<sup>16</sup> An early decision by the CONTRACTING PARTIES held that consultations under Article XXII:1 would be considered as fulfilling the consultation requirements of Article XXIII:1. BISD 9S/20.



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any relevant source they deem appropriate and they sometimes consult experts to obtain their technical opinion on certain aspects of the matter. Panels may seek advice or assistance from the secretariat in its capacity as guardian of the General Agreement, especially on historical or procedural aspects. The secretariat provides the secretary and technical services for panels.<sup>17</sup>

Three years later, acting at a Ministerial Conference, the CONTRACTING PARTIES reaffirmed the 1979 Understanding and added more detail, including a requirement that, “The contracting party to which such a recommendation [i.e., to bring a challenged measure into conformity with GATT] has been addressed, shall report within a reasonable specified period on action taken or on its reasons for not implementing the recommendation or ruling by the CONTRACTING PARTIES.”<sup>18</sup> Further minor steps were taken in a *Decision on Dispute Settlement Procedures* on November 30, 1984.<sup>19</sup>

Dispute settlement under GATT was handicapped, however, by the requirement of Article XXIII that all matters be decided, and all action be approved, by the CONTRACTING PARTIES. GATT, in legal form, was a contract – a multi-party contract – and any decision to amend, modify, or interpret that contract required the consent of all of the parties.<sup>20</sup> In practice, this meant that the losing party in a dispute settlement proceeding not only could refuse to agree, and therefore “block” the adoption of an adverse report, it could even refuse to agree to the very establishment of a panel, thereby avoiding even the embarrassment of a panel proceeding.

Adverse GATT panel reports indeed were blocked by losing parties. In fact, parties who anticipated losing sometimes even blocked the establishment of a panel. It is a tribute to the system and the degree to which the parties valued it that blocking of both the establishment of panels and the adoption of their reports did not occur more often than they did. In fact, Prof. Hudec’s study shows that from 1947 to 1992, the losing party eventually accepted the results of an adverse panel report in approximately 90 percent of the cases.<sup>21</sup> Still, blocking was a problem and seemed to be occurring with increasing frequency in the 1980s. A significant step toward

<sup>17</sup> *Agreed Description of the Customary Practice of the GATT in the Field of Dispute Settlement* (Article XXIII:2), BISD 26S/215, 217, ¶ 6 (iv).

<sup>18</sup> BISD 29S/13, 15, ¶ (viii). <sup>19</sup> BISD 31S/9.

<sup>20</sup> In the absence of a specific rule providing otherwise, Article 40 of the *Vienna Convention on the Law of Treaties* requires unanimity among the contracting states.

<sup>21</sup> Hudec, ENFORCING INTERNATIONAL TRADE LAW, *supra* note 11, at 278.

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reducing the blockage – at least at the stage of establishing a panel – was taken with the adoption of the “Montreal Rules.” These grew out of a December 1988 Ministerial meeting in that Canadian city to review the progress of the Uruguay Round and to reap an “early harvest” of any completed results of the Round. Following further consideration in early 1989 in Geneva, the Montreal Rules were adopted by the CONTRACTING PARTIES in April of that year.<sup>22</sup> They formed the basis of what eventually became the *WTO’s Understanding on Rules and Procedures Governing the Settlement of Disputes*.

The CONTRACTING PARTIES agreed to apply the Montreal Rules “on a trial basis from 1 May 1989 to the end of the Uruguay Round in respect of complaints brought during that period under Article XXII or XXIII.”<sup>23</sup> The most significant portions of the rules were those that placed time limits on consultations and that provided further for the automatic establishment of a panel. Parties to which a request for consultations had been made under either Article XXII:1 or XXIII:1 would be required to reply to that request within 10 days, and to agree to enter into consultations in good faith in no less than 30 days. In the absence of an agreement to consult and the holding of timely consultations, the complaining party could proceed directly to request the establishment of a panel.<sup>24</sup> If consultations failed to settle the dispute within 60 days of the request, the complaining party then could request the establishment of a panel.<sup>25</sup>

Most significantly, in GATT’s all-too-typically indirect language, the Montreal Rules provided that, “[i]f the complaining party so requests, a decision to establish a panel or a working party shall be taken at the latest at the Council meeting following that at which the request first appeared as an item on the Council’s regular agenda, unless at that meeting the Council decides otherwise.”<sup>26</sup> This meant that a panel would be established, without fail, at the second meeting of the GATT Council after the request was put on the agenda, unless the Council decided otherwise. For the Council to decide “otherwise” under GATT’s process of decision by consensus, however, all parties – including the complaining party – would have to decide “otherwise.” In other words, the system had changed from one that required consensus – “positive consensus” – to establish a panel to a system of “negative consensus” – a system that required consensus not to establish a panel.

<sup>22</sup> *Improvements to the GATT Dispute Settlement Rules and Procedures*, Decision of 12 April 1989, BISD 36S/61 (hereafter “Montreal Rules”).

<sup>23</sup> *Id.* ¶ A.3.    <sup>24</sup> *Id.* ¶ C.1.    <sup>25</sup> *Id.* ¶ C.2.    <sup>26</sup> *Id.* ¶ F.(a).