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MTN and the Legal Institutions of International Trade

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SUBCOMMITTEE ON INTERNATIONAL TRADE

ABRAHAM RIBICOFF, *Chairman*

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MTN And The Legal Institutions of International Trade

MEMORANDUM

May 31, 1979

FOR: The Committee on Finance, United States Senate

By: Professor John H. Jackson, University of Michigan Law School

RE: Impact of the Multilateral Trade Negotiations: on the Institutions of International Trade

NOTE: This memorandum, requested by the Professional Staff of the Senate Finance Committee, is based on the agreements resulting from the Multilateral Trade Negotiations, as contained in Joint Committee Print WMCP:96-18 of April 23, 1979.

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I. Introduction

It is an impressive accomplishment. As the seventh major trade negotiating round in the context of GATT, (the General Agreement on Tariffs and Trade) this Multilateral Trade Negotiation or "MTN" as it is often called, may well live up to the claim that it is the most far-reaching of any of the trade negotiating rounds, except perhaps the first, when the GATT itself was drafted in 1947. The 1954-55 "Review Conference" to overhaul GATT was extensive but not nearly as wide ranging or as innovative as the current MTN. The 1962-67 Kennedy Round was very extensive with regard to tariff matters, but failed to achieve significant changes in international rules on non-tariff barriers (NTBs). The MTN, however, is the first negotiating effort since the GATT was originally drafted, to address significantly and broadly a number of NTB questions. This is no small achievement, since NTBs are much more difficult to negotiate than are tariffs.[1]

The MTN results are particularly impressive for a negotiation coming as it did during a time of trauma for the international economic system, as well as a time of economic "stagflation" coupled with narrow parliamentary majorities for the governments of virtually all of the major participants in the negotiation. Considerable commentary has been published about the "protectionist trends" in the world during the last half decade. It has not been a time of farsighted leadership. The negotiation results bear the scars and blemishes of the gauntlet which it had to run. But for the first time since the original GATT, there has been a major extension of international discipline for non-tariff barriers.

Apart from the impact of the MTN on trade and other economic policies, and apart from the obvious impact that the MTN will have upon U.S. law and government structure, it is clear that the MTN has important implications for the "constitution" of GATT, i.e. for the general "legal-instutional" structure of international trade. As requested, the focus of this memorandum will be upon this latter topic. For example, will the MTN results strengthen or weaken GATT as an institution for coordination of international trade policy and resolving disputes over that policy? Will the MTN result in a shift of power allocation within the GATT structure? Will important institutional weaknesses of the GATT system likely be corrected, improved, or exacerbated by the MTN results? Will the old GATT rules or the new MTN rules be more or less likely to be followed as a result of the MTN? What, if any, impact will the MTN have on the ability of the GATT as an institution to cope with trade and economic problems or crises that may arise in the next decade or two?

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1. This due to at least three factors: 1) their complexity and subtlety, requiring a high degree of expertise even to identify the practices which might operate as NTBs; 2) the difficulty of appraising the effect or concrete impact on trade, of either an NTB or an international rule regarding an NTB, thus making it difficult for national representatives at a negotiation to evaluate the "quid pro quo" or reciprocal balance of any set of obligations; and 3) the divergence of governmental and economic philosophies represented at the bargaining conferences, such as to render it impossible to have agreement on fundamental goals or assumptions (reduce government interference and regulation, or allow greater government control of economic transactions? further liberalize international trade or only "organize" it?).

These and a number of other questions, will be the subject of this memorandum. Simple answers often cannot be provided, however. The most that can be done at this time of the birth of the "GATT-MTN System" is to offer some perspectives of history, some tentative prognoses, and a number of questions to be answered only in the future. This memorandum cannot provide even these for all impacts of the MTN, however, and for elaboration on some of the points to be made, the reader is referred to other works.[2]

II. Some General Perspectives

A. The General Agreement on Tariffs and Trade

At its origin the GATT was never intended to play the role it has been forced to play. It was conceived as principally a reciprocal tariff reduction agreement, to be appended as a subsidiary set of obligations to the ITO (International Trade Organization.) The GATT general clauses were drafted to prevent avoidance of the tariff commitments by other means, and a bare minimum of institutional measures were included in the GATT. When the ITO failed to come into being in the late 1940's due to opposition in the U.S. Congress, the GATT became the only viable international institution for helping nations to resolve their international trade policy differences, and thus the GATT began to evolve into the central international institution for trade, which it is today. This uncertain beginning explains many of the defects and difficulties of GATT. In fact the GATT has served world trade and economic well-being far better than anyone had a right to expect. But in the last decade, a number of its constitutional infirmities have begun to catch up with it, as international economic interdependence, the quadrupling of GATT membership to include countries with greatly divergent stages and theories of economics, and the crises of energy costs and unemployment, have all buffetted the GATT.

Some of the weaknesses of GATT can be mentioned here, to help paint the background for later portions of this memorandum. For brevity's sake let me list them:

1) It is difficult if not impossible to amend the GATT. Thus it has not been possible to keep GATT specific rules relating to trade up to date.

2) Partly because of this, but also for a number of other reasons, compliance with GATT rules has been faltering. Some GATT rules are

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2. See for example, other works of this writer and works cited therein: World Trade and the Law of GATT, Bobbs-Merrill Co., Dec. 1969; "The Crumbling Institutions of the Liberal Trade System", J. of World Trade Law, Vol. 12, No. 2, p.93-106, March-April, 1978; "The Jurisprudence of International Trade: The DISC Case in GATT", Amer. J. of Int'l Law, Vol. 72, No. 4, p.147-781, Oct. 1978; "Governmental Disputes in International Trade Relations - A Proposal in the Context of GATT" J. of World Trade Law, Vol. 13, No. 1, p.1-21, Jan.-Feb. 1979; "The General Agreement on Tariffs and Trade in United States Domestic Law," 66 Mich. Law Review, p.249-332, Dec. 1967.

virtually ignored (in some cases because such rules have been found to be ill-suited to current problems).

3) The dispute settlement procedures of GATT have not been working well, for a variety of reasons explained elsewhere. (See V below).

4) The GATT decision making structure is awkward and not well designed to reflect needs of the participants, or to create new rules which would likely be effective.

5) Significant changes in GATT rules have had to await major "trade negotiating rounds," which have been further and further apart (about a decade between the last two). Thus pressing issues are delayed until they can be taken up in the context of a major round. There is a growing tendancy of GATT nations to preserve their "bargaining chips" and maintain measures damaging to the trade of others, longer than would be the case if changes did not have to await a "trade round."

6) Trade in agriculture goods has never really followed GATT rules, because of explicit or tacit exceptions including rule non-compliance. Numerous ad hoc measures have been tried, to help manage the problems of international trade in agriculture, but without much success.

7) The most-favored-nation (MFN) clause of GATT, mandating non-discriminatory treatment of trade, was originally a central policy of the GATT rules. Over the years this principle has been eroded by both industrial and developing countries, through expansive application of explicit GATT exceptions("loopholes") or through tacit acquiescence to non-compliance.

8) The uneasy relationship of developing countries' trade (exports and imports) to GATT rules has always been the subject of dispute and acrimony. The growing industrial capacity of some developing countries promises to put additional strain on the adjustment capabilities of industrial countries, and this too poses problems for the traditional GATT rules.

Some of the questions addressed in this memorandum are: What impact will the MTN results have on <u>these</u> weaknesses of GATT?

B. The MTN Results

The most striking feature of the MTN results is the series of "codes" or agreements on particular non-tariff measures affecting international trade. These include agreements on:

1) Subsidies and countervailing duties

2) Antidumping duties

3) "Technical barriers to trade" relating to national product standards

4) Government procurement

5) Procedures for licensing of imports, when licensing is permitted

6) Valuation for customs purposes

7) The "Framework" of GATT, with sub-parts relating to developing country priviledges and obligations, balance of payments measures, and dispute settlement procedures.

8) Agreements concerning agriculture products, including Dairy and Beef products.

9) A Safeguards Code may later be completed.

Upon reading the whole set, one is struck by the remarkable complexity and far reaching scope of some of these agreements. The willingness of nations to yield "sovereignty" (if that is a meaningful concept) on such subjects as government procurement, is impressive. Yet the overall impact is perplexing. This variety of agreements, and the variety of approaches to substantive and institutional questions, reflect a somewhat fragmented approach to the negotiation. It is difficult to discover an overall consistent policy, particularly on the questions to be addressed by this memorandum (institutional and legal). Even on a number of substantive issues, however, there seems to be a variety of approaches, probably reflecting different objectives of national domestic interest groups which made their influence felt on different parts of the negotiation. Because of the complexity of the whole, of course, negotiating had to proceed in subgroups. Yet as currently drafted, the agreements vary widely on such matters as dispute settlement, or degree of precision in rule statements, or the extent and nature of international decision-making authority. On some important common substantive issues also, different agreements seem to take differing approaches: Some seem tuned toward the direction of trade liberalization to increase the flow of trade, others seem more trade restricting; some seem to enhance MFN, others to further erode it; some seem designed to further limit governmental interference with international trade, others to establish new mechanisms by which governments and international bodies can "manage" that trade.

Later portions of this memorandum will discuss in greater detail the "constitutional" or "legal institutional" questions of the MTN impact. Before turning to those, however, a brief comment about several overall substantive policy implications of the MTN results might be useful.

First: Explicit or carefully-considered responses to a number of the truly "tough questions" posed by GATT weaknesses outlined above have been avoided or "ducked". This is perhaps understandable - to achieve any agreement at all may require evading many tough issues. Yet one must recognize that many of these issues remain with us, and may even be more perplexing as a result of the MTN. Some of the comments below, as well as those in later parts of this memorandum will illustrate this point.

Second: The question of how to solve international trade problems can be approached from divergent philosophies: on the one hand a "freer

trade" or nongovernmental approach, i.e. to create international rules generally designed to minimize government interference or particular discretionary interference; on the other hand a more "managed" approach which may be called "organized free trade" or "dirigisme", pursuing the idea that governments shall be given power to get together and direct or manage the type and amount of trade which can flow. The original GATT was drafted to reflect views suggested by the first approach above. The overall results of the MTN, however, have many features which suggest more of the second approach than the first. The agriculture agreements (not unexpectedly) lean in this second direction. The creation of new "Committees" in many of the codes may also lean in this direction. Portions of the Subsidies-Countervailing Code (establishing diplomatic consultations and authorizing agreements between nations to reduce exports, raise prices, or otherwise minimize "injury" to competing producers) suggest a similar approach. In fairness, however, it seems that other agreements (Government Procurement, Standards, Customs Valuation) may be more in tune with the first approach, i.e. the traditional GATT view of restricting governmental interference in the international market.

Third: The erosion of the MFN policy of non-discrimination seems to be carried even further by the MTN. The Framework agreements seem to perpetuate and extend important deviations from MFN on behalf of developing countries. The restriction of some Code benefits to "Code signatories" also makes inroads into the general concept of MFN. Certain "selectivity" approaches towards safeguards on escape clause actions may make further inroads. These inroads do have some policy justifiactions. The question which must be asked is whether the general policies favoring MFN have been adequately weighed against the particular desires in certain contexts to depart from MFN.

Fourth: The tough overall question of how best to manage international trade in agricultural products seems largely unresolved, although some particular attempts to nudge agriculture into the general discipline of international trade rules can be found (e.g. in the Subsidies-Countervailing Code).

Fifth: At least some perplexing questions of developing country trade seem primarily handled by a "legalization" of currently tolerated non-compliance practices of those countries, the extension of the legal opportunities of those countries to deviate from GATT rules, and an expression of desire that developing countries will "graduate" to the more significant GATT and MTN rules of trade.

Finally, one more general remark: Many important provisions of the MTN agreements are loosely worded. Either they are expressed as "hortatory" admonitions, or vague terms are used. Lack of precise agreement in some areas may have necessitated the use of ambiguous phrases to "paper over" disagreements. In addition, the institutional means to gradually develop precision in these areas is not well established. Consequently much could depend on how government officials in the next few decades go about the application of the MTN rules and principles. To negotiate such loosely worded statements may be acceptable to those who view problems from the perspective of a governmental official who believes in his own good faith and wants to give government officials some leeway in the operation and management of the difficult problems they may face in the

future. Yet the risks of this approach must be recognized: less predictability for both government and non-government decision makers; politicization of government decisions on trade matters; distortions in the market processes; a heavier administrative burden on government agencies and a likelihood that a larger number of trade matters must be regularly considered by higher ranking government officials, (congressional or executive). Implementing national legislation can, of course, provide a higher degree of precision to the rules at least as applied by the nation concerned. There is a risk then, however, of different nations applying the rules differently.

III. The Legal Structure of International Trade

The weak constitutional structure of GATT is perhaps typified by the fact that GATT as such, has never come into force. It is applied only through the Protocol of Provisional Application, which was originally designed to apply GATT for a short period of time until the ITO came into force and GATT could be applied "definitively," events which never occurred. The Protocol exempts from most GATT requirements "existing legislation," thus creating the so-called grandfather rights.

It has already been stated that because of the history of its origin, the GATT has only minimal institutional clauses. For these and other reasons the GATT has managed with a small secretariat, and has usually not had the luxury of sub-bodies with delegated authorities and legally specified procedures, which one finds in the International Monetary Fund, or other organizations. The GATT has created sub-bodies and procedures, but only those which could be justified as "interpreting" or carrying out the broad words of GATT.

Amendments to GATT require a treaty-protocol process with at least two-thirds of the members acceding to the amendment. Even then the amendment does not apply to those who don't accept it. Some parts of GATT require unanimous approval to amend. As a consequence of these clauses, the four-fold increase in membership, the divergence of member interests, and the understandable reluctance of some national executive authorities to exert the political effort required to get treaty approval by their parliaments on matters which little concern their country, it has been increasingly assumed that amendments to GATT, possibly except those of great interest to the developing nation majority, are virtually impossible to obtain. Certain 1955 amendments requiring unanimity never came into force. The 1964 amendment adding Part IV to GATT which contains a set of general policy statements favoring developing countries, was the last formal amendment of the GATT general clauses.

Other ways to change the system have had to be found. One such is the use of "waivers" under GATT rules, which require only "votes." Some waivers have had virtually an amending effect (e.g. waiver for U.S. agriculture restrictions; waiver for the Generalized System of Preferences).

Another technique for change is simply to negotiate a separate treaty agreement concerning matters otherwise governed by GATT. Sometimes, as

with the 1967 Anti-Dumping Code, such agreement is called an "interpretation" of a GATT clause. Other times, such as in the various textiles arrangements, the agreements have measures inconsistent with GATT rules, even though the agreement may provide that it does not prevent any nation from asserting its regular GATT rights.

Yet another approach to the need for change of a GATT rule is to simply not comply with it! Instances of non-compliance have apparently been growing in the last decade, and in some cases these are tolerated. Repeated examples of tolerated deviation from one rule tends to develop into a "de facto" situation under which it is understood that the rule can be largely ignored. Such is the case, for example, with the use of a "tariff surcharge" for balance of payments reasons, despite the fact that it is not usually permitted by GATT.

A number of legal-constitutional problems coexist with the types of practices mentioned above. Basically they cluster around the notion that the legal obligations are decreasing in force as time goes on, i.e. that non-compliance becomes an easier policy option for a government to consider as a way out of difficulties confronting it. When this happens, of course, the rules themselves lose part of their function. They no longer serve as a basis for government officials or private businessmen to predict trade patterns and opportunities. Investment decisions in developing as well as industrialized countries, for example, my be based on long term projections of trade opportunities. When decision makers cannot depend on governments refraining from interfering with trade, one basic purpose of the trade rules, to add to the certainty of an uncertain world in order to promote economic progress, has been lost.

Likewise, as rule departures become easier, another goal of the rules--to reduce tensions which can lead to political conflict among nations--becomes less likely to be fulfilled. Furthermore, tolerated noncompliance with rules can be misleading to a nation or enterprise which mistakenly takes a rule at face value. Greater expertise is needed by such nation or enterprise, or it may find itself at a disadvantage in the face of those who can manipulate the system to their advantage. When rules break down, the bargaining advantage of those already rich and powerful may be significantly enhanced.

What then, in the broadest sweep of policy analysis, can be said about the impact of the MTN on these matters of "GATT jurisprudence?"

It seems clear that the MTN has not explicitly addressed itself to most of the problems above, except in a few cases to create agreements designed to make legal (or quasi-legal) practices which had heretofore been tolerated illegalities. As currently drafted no provision is made to improve the GATT legal structure, to provide for definitive application, to regularize the "grandfather rights" (although the subsidies-countervailing code will greatly affect the most important grandfather right of the U.S.), or to decrease the number of current GATT rule departures. All this is understandable, of course, and perhaps inevitable given the negotiating circumstances and bargaining strategies of the parties.

Even in those MTN clauses designed to introduce new legal rules, however, the MTN results may be compounding the legal complexities of the matter.

The MTN bargaining process and the resulting product of a series of codes which are virtually "stand alone" treaties in themselves, have an overall impact on the GATT legal system. The interrelationships between the various codes and the GATT becomes increasingly complex, however. Such complexity makes it harder for the general public to understand the "GATT-MTN system," and thus may result in less public support for that system over time. The complexity will also make it harder for those countries which can devote less governmental expertise to the GATT representation problems. In addition, such complexity will inevitably give rise to a variety of legal disputes among the GATT parties. It may also contribute to beliefs that the richer nations can control or manipulate the GATT system for their own advantage.

It should be noted that many (maybe all) of these MTN technical legal problems with GATT may be fully justified as fulfilling important policy objectives in the face of the rigidity and unamendability of GATT and in the face of its inadequate constitutional structure. In each such case, however, it must be recognized that there is some cost to the longer term usefulness of GATT and related agreements. That cost may be worth it. What is suggested by this discussion and the discussion below, however, is that there are a great many important unresolved issues left over from the MTN, which will require considerable effort in the years ahead.

Finally, because the various codes differ so much in approach, and contain a variety of institutional and separate dispute settlement provisions, the administration of, and national representation to, these code institutions will be more costly. It is also more likely that there will develop a series of "mini-GATTs": one for Government Procurement, one for Standards, one for Subsidies, etc. with government personnel developing specialized competence for their own "mini-GATT". This can lead to bureaucratic in-fighting to protect jurisdictional "turf" (at the secretariat and at national capitals), and to reduced transferability of personnel skills from one "mini-GATT" to another, such as might be needed to conduct dispute settlement cases, or meet new problems arising in the next decades.

In short, the MTN results will assist in the further "Balkanization" of international trade policy.

IV. Institutional Structure: Decision Making And Secretariat Services

The "legal context" of a set of rules includes at least two important institutions: an institution (or set of institutions) for creating new rules or changing old rules, i.e. a "rule making" institution (such as a parliament); and an institution (or procedure) for applying rules and resolving disputes about them (e.g. courts or tribunals). It is likely that rules without these two institutions will become ineffective.

This part will discuss the question of "rule-making" and decision making in general, in the international trade system. In Part V, rule application and dispute settlement will be discussed.

The GATT decision making structure is not elaborate, to say the least. The GATT provides for the "CONTRACTING PARTIES" acting jointly on such matters as delegated to them under the agreement and "generally, with a view to facilitating the operation and furthering the objectives of this Agreement." (This remarkably broad and ambiguous language has, on the whole, been cautiously used.) The GATT provides that each contracting party shall have one vote, and that on most issues a majority vote shall prevail.

In general the GATT does not use the above described decision making authority for "rule-making." The tradition of GATT is that new obligations (tariff commitments or new rules) are binding only on those who accept them as part of a newly negotiated treaty instrument. The waiver power under GATT, however, allows a special two-thirds majority of GATT to waive obligations, and in some cases a waiver could arguably amount to changed obligations (or benefits) for a party, against its desires. Particularly, waivers from MFN could have this result. Some waivers may grant privileges conditioned upon certain obligations (such as consulting) and these too have a certain de facto effect of creating new rules, (such as the consultation procedure.)

Clearly a troublesome problem with this decision making process, at least from the point of view of the United States and certain other countries, is the one-nation one-vote procedure which exists in many international organizations. The International Monetary Fund, by way of contrast, has a system of weighted voting which broadly recognizes economic contributions to the IMF and economic power generally. (Similarly the IBRD, IFC, IDA have weighted voting, and many commodity agreements have weighted voting systems which equate consumer nations with producing nations.)

In GATT the U.S. has only one out of more than 80 votes, while two other important blocs have substantially larger votes.

The EEC member states are all GATT contracting parties, giving the EEC nine votes in GATT.

The L.D.C.s number over two-thirds of GATT, thus having enough votes for a waiver, or to amend GATT.

The EEC votes when combined with the EEC Associated states (Yugoslavia, Spain, etc.) and the E.F.T.A. and Lomé allied countries, total over two-thirds of GATT. At least theoretically, therefore, on some issues this bloc would have a commanding influence.

It is sometimes argued that votes are not often used, that instead "consensus" is reached, and therefore attention need not be given to formal voting strength. The problem with that reasoning, of course, is that the bargaining and compromise which goes on in order to reach a consensus does so at least partly in the light of the potential vote which could occur if negotiations break down.

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New GATT obligations, as indicated above, are generally negotiated as new agreements, often in the context of one of the major "trade negotiating rounds" like that of the MTN. In the MTN as in previous similar cases, there developed "key country" groupings. On some matters the critical decisions depended only on the U.S. and the EEC. Other decisions included more participants. Clearly such a "bargaining" system gives the large powers great weight. Indeed the risk in this type of system is that the small or weak nations may not be consulted at all (until too late) or may have little opportunity to protect their interests.

Attempts have been made to improve the GATT decision process. In 1960 a "Council" was set up by GATT decision, to meet almost monthly and prepare decisions for nations to vote. Without provisions in the GATT on the matter, however, it was felt all GATT members should have the right to participate in the Council and all decisions could be appealed to the CONTRACTING PARTIES, acting jointly, preserving the basic GATT voting situation. In 1975 a "Consultative Group of 18" was set up in GATT, again as a way to strengthen the coordination and decision making of GATT. It appears that this group has not been very influential.

The basic problem remains - how, in the face of a larger and more diverse membership, can GATT decision making be made more efficient and effective? As long as it is subject to the disparity between real and voting power and the other anomalies of a one-nation one-vote system, it seems unlikely that powerful nations will entrust that system with any meaningful authority. Clearly great opposition to any change exists, however.

The MTN largely ignored this institutional question. A "GATT Reform" group was set up to negotiate reforms, but did not come to any conclusions on these decision making issues. However, the MTN results do affect the GATT decision making process, possibly in very significant ways. Almost all of the new Codes create a new international body, called a "Committee of Signatories" or a "Committee on Government Procurement," and the like. (Several agreements call for committees" in the framework of GATT," which may not be new legal entities.) In the agreements the composition of these committees is generally the same: each "signatory" or "adherent" or "party" is entitled to one representative. Voting is not generally mentioned, a striking omission! Thus it is at least within the realm of possibility that a one-member-one-vote practice could develop, and a majority vote prevail. Mostly these committees have only consultative powers, but some have important powers in the dispute settlement procedures (also set up under each Code).

Several observations can be made, and some questions posed. The creation of this new set of international bodies could have some interesting impacts. Clearly one impact will be to take away from the GATT CONTRACTING PARTIES as such, some authority. Decision making will be less centralized than before. Even if all these Committees meet in GATT headquarters and depend on the GATT for secretariat services, there will be created a series of new legal entities, each presumably excluding some members of GATT from its deliberations. In its favor it can be said that such exclusiveness may be useful in encouraging more nations to join each Code, or at least to exclude from voting those who have no interest

in the subject matter. On the other hand, in addition to adding to the administrative burdens of national and international government, such exclusiveness may make it more difficult for some Code non-signatories to achieve a "right to be heard" so as to remind Code signatories that actions they take may impinge unnecessarily on others.

Consequently it appears that while the total GATT-MTN system may have been strengthened by the remarkable increase in scope due to the new rules negotiated, and the setting of a new group of committees and procedures in the GATT "context", the GATT CONTRACTING PARTIES, Council and other GATT bodies, may have been weakened. Whether this is good or bad depends on various points of view and on future developments.

What can be said about these various Code Committees? It is impossible at this time to know what will be the composition of these Committees, except that it is fairly clear that the industrialized "OECD" nations are likely to belong to most of them. Presumably some LDC countries will belong. Thus it appears likely that at the outset, the industrialized countries will have much greater influence in these committees vis-a-vis the LDCs, than would be the case in GATT itself. However, the United States may not find this always an advantage.

As presently worded, a number of these code committees could technically have representatives from the European Economic Communities as well as each of the nine EEC member states, a total of 10! Hopefully the EEC would not exercise a voting power of ten, but one can see at least some potential risks for United States international trade relations.

Even in cases where the relevant Committee has no formal decision-making authority, as the only official international agency to oversee the operation of a new code, it is likely to have considerable influence, particularly in early years, over the process of interpreting that code.

As years go by, more nations may join the Codes. In some of them they may do so by right, i.e. no vote or other procedure is needed. It could happen, therefore, some years from now that an entirely new majority will be in control of some of these key committees. In some Codes this could have substantial impact on the degree to which such nations will be obligated to or will comply with the rules of the Code.

These developments should not be overemphasized, of course. Little decision making power apart from the disputes procedures has been given these Committees. Yet it seems clear that at best the MTN results have not improved the GATT system decision making structure, at least from a long term perspective. The advantages of the MTN may still outweigh these disadvantages, but this analysis demonstrates how little priority seems to have been given in the MTN to basic institutional problems, and suggests that the work is completed neither for the international community nor for the United States government itself. For the United States government to successfully manage its economic interests in the difficult diplomatic milieau which it has helped create, will call for considerable improvement in its internal organization and marshalling of diplomatic skills.

Another institutional issue which must be considered is that of the Secretariat. Secretariat services are always an important but sometimes overlooked ingredient of effective international institutions. As described earlier, the GATT has operated with a comparatively small secretariat, partly because of its uncertain constitutional status as an "organization." Indeed technically the GATT has no secretariat but "leases" a secretariat from the ICITO (Interim Commission for the International Trade Organization.)

The new MTN "Codes" or agreements say very little about the secretariat. Many of them simply state that "This agreement [code, arrangement] shall be serviced by the GATT Secretariat."

Clearly the number of new committees, dispute settlement procedures, rules to apply and the substantial addition of subject matter to the GATT-MTN system, will require extensive new secretariat capacities (as well as, incidentally, substantial increases in national government agency staff to participate in the work of the new system and guard national interests.)

Attention will have to be given to a series of practical questions, including:

1) How will the new services be financed? Through the general GATT budget, or through specific budgets and specific contributions by the signatories of each Code?

2) Will the expanded GATT secretariat be able to attract and hold capable people? How will they be selected?

3) Will the secretariat have the capacity to assist nations in identifying problems before they become crises?

4) To what extent will the secretariat need to develop additional capabilities to assist and counsel national representatives from smaller or less affluent countries which cannot afford the expertise and specialized representation necessary to guard their national interests in the greatly increased complexity of the new GATT-MTN system?

V. Rule Compliance and the Dispute Settlement Procedures

A. Rule or Power Oriented Diplomacy

The true effect of international legal obligations or "rules" has for centuries been the subject of comment and perplexity. As the world becomes smaller and economic interdependence increases, the question of the role of those international rules which relate to national government economic activities becomes increasingly important. Unlike many international "rules", those relating to trade directly affect many private citizens or other economic entities whose

decisions may depend on whether the rules are adequate predictors of governmental behavior. Traditional approaches of diplomacy, which may suffice when international dealings are primarily government-to-government (such as many military or defense matters) or when the rules are intended to be "guidelines" rather than legal obligations (such as some rules for "human rights" or cultural activity, , may not be adequate to the task of operating a complex international economic system with its large number of actors and decision makers, the many organized and competing interest groups, the uneasy relationship between Parliament or Congress and the Executives, and the inevitable difficulty of keeping major actions secret. Rules can take on important and different functions in this context: facilitate decentralize enterprise decisions, allow a myriad of detailed actions to be taken at lower levels of government officialdom thus sparing higher authorities, giving governments some arguments to counter parochial short term private interest group demands which can have long range damaging effects on national and world economies. Particularly the nature of rules becomes influenced by, and creates influences on the dispute settlement processes as part of the overall "legal system" in which the rules are set. In Part IV of this paper the focus was on the rule making processes; in this part the focus is on the "rule applying" processes.

In broad perspective one can roughly divide the various techniques for the peaceful settlement of international disputes into two types: settlement by negotiation and agreement with reference (explicitly or implicitly) to relative power status of the parties; or settlement by negotiation and agreement with reference to norms or rules to which both parties have previously agreed.

For example, countries A and B have a trade dispute regarding B's treatment of imports from A to B of radios. The first technique mentioned would involve a negotiation between A and B by which the more powerful of the two would have the advantage. Foreign aid, military maneuvers, or import restrictions on other key goods by way of retaliation would figure in the negotiation. A small country would hesitate to challenge a large one on whom its trade depends. Implicit or explicit threats (e.g. to impose quantitative restrictions on some other product) would be part of the technique employed. Domestic political influences would probably play a greater weight in the approach of the respective negotiators in this system particularly on the negotiator for the more powerful party.[3]

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3. See generally, Jackson, "Governmental Disputes in International Trade Relations - A Proposal in the Context of GATT", Journal of World Trade Law, Vol. 13, No. 1, January/February 1979.

On the other hand, the second technique suggested - reference to agreed rules - would see the negotiators arguing about the application of the rule (e.g. was B obligated under a treaty to allow free entry of A's goods in question?). During the process of negotiating a settlement it would be necessary for the parties to understand that an unsettled dispute would ultimately be resolved by impartial third party judgments based on the rules, so that the negotiators would be negotiating with reference to their respective predictions as to the outcome of those judgments and not with reference to potential retaliation or exercise of power of one or more of the parties to the dispute.

In both techniques negotiation and private settlement of disputes are the dominant mechanisms for resolving differences; but the key is the perception of the participants as to what are the "bargaining chips". Insofar as agreed rules for governing the economic relations between the parties exist, a system which predicates negotiation on the implementation of those rules would seem for a number of reasons to be preferred. The mere existence of the rules, however, is not enough. When the issue is the application or interpretation of those rules (as compared with the formulation of new rules), it is necessary for the parties to believe that if their negotiations reach an impasse the settlement mechanisms which take over for the parties will be designed to fairly apply or interpret the rules. If no such system exists, then the parties are left basically to rely upon their respective "power positions", tempered (it is hoped) by the good will and good faith of the more powerful party (cognizant of his long range interests).

B. The GATT Dispute Procedure and Its Problems

As observers of international trade and economic relations readily notice, the existing mechanisms for the resolution of trade and other economic disputes in international affairs leave much to be desired. Under the GATT agreement various provisions in a variety of articles of GATT provide for various techniques of resolving differences among trading partners. Some of these techniques are really processes by which the parties agree on new norms or new rules, such as negotiations in a major tariff and trade liberalization "round." Other techniques, such as those in the escape clause of Article XIX of GATT comtemplate reciprocal or retaliatory type action on the part of the aggrieved party to "offset" or "compensate" for the trade damage occasioned by the other's activity (in this case a permitted activity.) In any system of international trade rules, such techniques will continue, and will in many cases be the central if not the exclusive process of resolving differences as to what rules <u>should</u> be, or redressing imbalances that occur from permitted activities under the rules.

In this memorandum, however, focus will be upon the type of dispute that involves the application and interpretation of a previously agreed

norm or rule such as a "tariff binding" or a rule regarding the circumstances which permit a country to apply a countervailing duty to the imports from another country. Many of the GATT disputes of this type fall under the central dispute resolution mechanism of Article XXII and XXIII (Article XXIII calling for a procedure possibly culminating in a voting action by the ruling GATT body, the CONTRACTING PARTIES.) While this procedure had considerable promise in the early decades of GATT history, in recent years it has become apparent that the procedure is inadequate. Many governments have hesitated or refused to invoke the procedures of Article XXIII. This hesitation stems partly from a lack of faith in the fairness of the process, particularly since in many ways an imbalance of power between the disputing parties tends to bias the dispute resolution mechanism. A small country, even if allowed to retaliate against a large country, appropriately doubts that such retaliation would have any concrete effect on the large country.

There are a series of other weaknesses involved in the GATT mechanism outlined in Article XXII-XXIII. In many cases a dispute is subject to inordinate delays. A "footdragger" has many procedural opportunities to slow down the process. In some circumstances a dispute, whether or not brought under the mechanism of Article XXIII, "festers on" for many years with no resolution.

Part of the Article XXIII process has been a tradition of appointing "panels" of persons who are not citizens of either of the disputing parties to "hear the case" as presented by the disputing parties, and come to some conclusion. This tradition of panels was a welcome innovation in the early years of GATT history, but it has not been sufficiently developed and it is posing a number of problems in recent years. For one thing, it has become increasingly difficult to obtain the services of appropriately trusted persons to sit on these panels. This is partly due to the tradition of selecting them from the officials who represent governments to GATT - a busy group. Likewise, the fact that usually each of the persons on the panel, although ostensibly acting in his individual capacity, nevertheless is an official representing his country in GATT makes it difficult if not impossible for him to view his actions in such a panel as insulated from the influences of his government's foreign economic policy, and consequently the relationship of that government to other countries in the world, including the disputing parties.

The panels have also been weakened with tasks that are probably mutually conflicting or beyond their competence. To a certain extent the panels have tried to play the role of conciliators between the disputing parties, to urge them to come to an agreement about the dispute. In so doing, the panel often is assisting the negotiation with reference to the <u>power</u> positions of the respective parties, and not only with reference to whether an agreed rule favors one or the other party. At a later stage, absent agreement between the disputants, the panel is called upon to write a report for the CONTRACTING PARTIES in which it may determine whether a GATT rule has been "breached." However, under the provisions of GATT Article XXIII, it is not merely or even necessarily a breach of a GATT rule which is critical; it is "nullification and impairment". This is a vague and ambiguous concept

which relates to "damage" to the complaining nation's trading "expectation" under the GATT agreement.[4]

The ambiguities of the "nullification and impairment" concept, as well as the implied invitation to act "ex aequo et bono" or in an "equitable" as opposed to a "legal rule application" manner thrusts a considerable burden on the panel, one that it is probably not competent to undertake. Similarly, the panels often assume a duty to make a recommendation in the dispute. Such recommendations can be political or "rule making" in nature, as opposed to merely establishing whether and how a previously agreed rule applies to a situation. This, too, forces the "judges" to play a political role, detracting from the appearance of impartiality of the panel.

Thus, the GATT dispute mechanism enjoys less than great confidence by parties of GATT.[5] The uncertainties of the process, plus the suspicion of taint of political and power influences, often render the mechanism suspect, and arguably makes it simply a conciliation process in a negotiation between the disputants.

Other weaknesses include: 1) The procedures for initiating a complaint process are ill defined, subject to delay and arguably subject to "permission" of a political body through vote of the Contracting Parties (which may in practice necessitate agreement of the disputants); 2) The delay plays into the hands of a "fait accompli" approach to

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4. Partly as an attempt to remedy the ambiguity of GATT Article XXIII, a concept of "prima facie nullification" has been developed. This concept applies in certain cases, namely: i) a breach of the GATT legal obligations; ii) the establishment of a quantitative restriction on imports; or iii) establishing a new subsidy for domestic production of a product for which a previous GATT tariff "binding" was undertaken. If a prima facie case is established, then the theory is that the burden shifts to the infringing country to show under GATT Article XXIII that there has been <u>no</u> nullification and impairment. Although an ingenious addition to the GATT jurisprudence, the prima facie concept is still subject to criticism. Even in such a prima facie case, the ultimate test under the Article XXIII procedures depends on the ambiguities of the phrase "nullification or impairment." For example, it is still not clear to what extent the breach by Country A of a rule gives rise to rights to another country B claiming potential or future harm from the illegal action. On the other hand, the prima facie concept may be abused to lead a panel to brand a country's action as Article XXIII "nullification or impairment" when only a minor technical breach of a rule has occurred and the culprit cannot prove that no <u>possible</u> nullification or impairment has occurred or could occur.

5. See, for example, criticisms of the GATT disputes procedures by government officials, summarized at p. 2 of Jackson, "Governmental Disputes in International Trade Relations - A Proposal in the Context of GATT," Vol. 13 Journal of World Trade Law p.1 (January/February 1979).

trade policy. A nation will argue that while its parliament or executive consider an action and before it is implemented, it is premature for an international body or foreign government to investigate or intervene. But after the action is taken, it is often unrealistic to undo it, since domestic political forces have already positioned themselves in its favor; 3) Meager resources of personnel, staff and money may contribute to inadequate consideration of the facts and arguments of particular cases; 4) Fact finding resources and procedures are inadequate; 5) There are inadequate procedures for reopening a complex case when a panel seems to have made a mistake; 6) The legal effect of "findings" of a panel are ambiguous; 7) Finally, the implementation phases of the procedures are too loose, too ill defined, and subject to the criticism that they involve political calculations and "trade offs" that are inappropriate to an adjudicating type procedure that needs to develop confidence and trust of future participants.

A valid and improved system should encourage settlement by the disputants, giving them assistance in the process of settlement, but it should encourage that settlement primarily by reference to the existing agreed rules rather than simply by reference to the relative economic or other power which the disputants possess. Clearly power will enter into the process of rule formation, but once the rules are formulated, they achieve their greatest utility if they in fact are applied and thus enhance the stability and predictability of economic relations, giving each party in those relationships the opportunity to rely upon those rules and compliance with them by others.

A revised dispute settlement mechanism should be built on modest expectations. For example, it should not be expected that all rules will be immediately complied with, or that all judgments of the disputes settlement mechanism will be immediately followed. However, the mechanism should be designed so that as time goes on, greater and greater confidence will be placed in the system, so that it will be more utilized, and so that gradually greater responsibilities can be put upon it.

The improved dispute settlement mechanism should separate the functions of a) conciliation, b) decision on the interpretation or application of the rule, c) rule or policy formulation, and d) recommendation or sanction. In order to establish that the dispute settlement mechanism relies primarily on reference to rules and their application, the fulcrum of a mechanism should be the establishment of an opportunity to obtain an impartial and trusted decision as to the interpretation or application of a previously agreed rule. To avoid tainting the process of that judgment, that is, to avoid reducing the trust placed in that decision because the process of obtaining it might be mixed with other goals, the impartial third party decision of rule interpretation or application should be (as it most often is in the various legal systems of the world) relatively isolated from other processes such as the process of assisting in negotiation for settlement, or the process of rule formulation.

C. The MTN and Trade Dispute Settlement Procedures

In the light of the comments made above, what can be said about the MTN results with regard to dispute settlement? The most striking characteristic is again the "Balkanization" or fragmentation of dispute settlement under the various agreements. The practicalities of negotiation procedures and tactics may have prevented the establishment of one centralized improved disputes procedure, but it should be recognized that a number of dangers are inherent in the fragmented MTN results:

a) The possibility of multiple overlapping procedures, with duplication of personnel and increased costs.

b) Multiple procedures add to the complexity of the total system, and mean that officials who must represent their governments in the system must learn a variety of procedures. Particularly for small countries that could be impossible, and consequently the system could be misused, or not used at all.

c) Informed public understanding of the dispute settlement mechanism would be greatly diminished, since its complexity would make it more difficult to explain or educate the public as to how the system operates. Consequently, some of the opportunity to develop prestige and trust in the system would be lost.

d) Countries may find ways to avoid or prolong procedures if a particular dispute seems to fit two or more processes. "Forum shopping" manipulations by disputants can develop.

e) There is likely to be an increase in the number of disputes about the procedures of each of the mechanisms, since the experiences of one system will not necessarily be considered as precedent for procedures in another system. By way of contrast, if there is a unified system, the procedural precedents will develop more quickly because the number of cases under the unified single procedure will be more than the number of cases under any one separate procedure would be. Consequently, the procedural tradition will progress more rapidly, can be given more attention, and should be better.

The Balkanization approach of the current MTN draft agreements has been carried into the disputes procedures with a vengence. No less than six new procedures for dispute settlement would be created by the MTN Codes and agreemtns, as they now stand.[6] In addition the "GATT

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6. These procedures and certain salient features of them are as follows:

1) Subsidies-Countervailing: Articles 12, 13, 16, 17, and 18:

Continued

Framework" agreements contain an elaborate exegesis on the current GATT disputes procedure. This procedure is referred to in several other agreements.

In most draft agreements there is language establishing (for each) a roster of possible persons to serve on panels, but some differences as to whether non-government personnel could be utilized. Most of the procedures have new clauses designed to guard against bias or conflicting interests of panel "judges" and against governmental interference. Unfortunately, however, some of the procedures invoke the ambiguous phrase "nullification and impairment and continue the unfortunate GATT practice of mingling the functions of "conciliation" with those of "adjudication," as well as "recommendation," leaving the duties of a panel relatively unclear.

It should be noted that decisions as to actual concrete actions or sanctions in response to rule non-compliance are never delegated to panels under the procedures, but are instead placed in the control of the various "Committees of Signatories" (which have been discussed in Part IV above.) When a panel's function is ambiguous or mingles functions of "conciliation" with those of "adjudication," the potential moral effect--which is usually the only effect--of a panel determination can be seriously weakened. The composition and voting structure of the Committees will likely have greater weight in the whole procedure, under such agreements.

It appears that the Code for Subsidies and Countervailing Duties goes the farthest in trying to reform the dispute settlement procedures of GATT, particularly in separating conciliation activity from the adjudicatory function. This reform, however, is attenuated by the ambiguity of much of language in this code.

(Consultation-Conciliation-Panel-Committee Procedures, with Committee decision at the end of the process.)

2) Standards: Articles 13 and 14: (Consultation-Panel procedures with an added provision for a "technical expert group".)

3) Government Procurement: Part VII: (Consultation-Conciliation-Panel-Committee procedures.)

4) Customs Valuation: Article 19 and 20 and Annex III: (Consultative-Conciliation-"Technical Committee"-Panel-Committee procedure.)

5) Anti dumping: Article 15: Consultation-Panel Procedures, followed by GATT type procedures as outlined in the "GATT Framework" agreement.

6) International Dairy Arrangement: Article IV: 6. Consultation, plus special convening of the "Committee."

Thus it seems clear that some improvements have been made (particularly as to time limits and Panel selection), but that little fundamental change or improvement can be expected because of the MTN agreements alone. The question of "rule" or "power" diplomacy has been compromised (perhaps necessarily, given the fundamental differences among governments), and familiar vague language and unclear or conflicting duties have been imposed on even the new procedures set up under the MTN results. Once again, the way governments choose to apply the system in the future will have great impact. This could make all the more important the structure of U.S. government responsibilities for safeguarding U.S. interests under the MTN-GATT system.

VI. Some Implications and Recommendations

Although this memorandum has pointed out a number of weaknesses in the results of the MTN as they relate to the institutions of international trade, it is not intended to unduely emphasize these weaknesses. In the overall perspective of the MTN results, and the extraordinary range of issues involved in the MTN, it was foregone that the U.S. negotiators would "win some and lose some." Attempts to provide more fundamental reform of the dispute settlement mechanism were probably not given a very high priority. In addition, the problem with difficult institutional questions in a negotiation involving large and often particular economic interests, is that no one country wants to spend precious "bargaining chips" pursuing negotiation goals which should, in the long run, be of advantage to all nations. The intransigence of some opposing negotiators also posed some difficult negotiating tactical questions for the U.S.

When weighed against some of the important successes of the MTN, an overall appraisal could lead to the conclusion that while lack of progress on the institutional issues is regrettable, such progress is "postponable" and not yet disastrous.

Nevertheless, the institutional questions, perhaps more than any other issues remaining left over from the MTN, demand more attention. These institutional questions could have the capacity for undoing the many years of difficult work of the MTN negotiators. The institutional problems could exacerbate the problems of world trade, the decline of discipline of the trade rules, and could place more pressure on national governments to seize short term trading advantage by various methods which can be seen by statesmen to pose longer term serious damage to the world economy. Attention is thus needed both to the <u>international</u> institutional structure for international trade, and to the <u>United States governmental</u> structure for international trade.

Regarding the international structure, further attention is needed on the process of keeping rules abreast of the fast changing developments in world economic realities, as well as to the problems of disparities in wealth within and among nations and the consequent dangers of peace-breaking tensions that could result. It is doubtful

that the world can wait for 10 or more years for another trade negotiation round, before giving serious attention to some of the deficiencies in the trading rules. It is doubtful that the world can afford to get along without the secretariat and consultation services of an international institution better designed to discover the facts of international trade and study the important alternatives for policy makers. Particularly with respect to the dispute settlement procedures, the United States in conjunction with several of its trading allies, could take important initiatives for improving the rules. A certain amount of experimentation could be undertaken, e.g. designing some model dispute settlement rules for implementation between several consenting nations pending such time as experience would demonstrate their usefulness to other nations.

One cause of some concern among thoughtful persons who are knowledgeable in international trade affairs, is the possibility that the United States government structure puts the United States at a disadvantage in the world trade system as it now operates. Several attributes of the United States governmental system are sometimes alleged to cause this result: The tension between the Executive Branch and the Congressional Branch (purposely designed in our checks-and-balances constitutional system) sometimes appears to damage United States negotiating efforts. In addition, and perhaps related to this point, the United States has a relatively "open" governmental structure, with elaborate provisions for citizen participation, open hearings, structured decision-making processes, etc. Such openness fulfills important governmental goals under the United States Constitution, but it renders the U.S. governemnt somewhat less flexible in its dealings on trade (and other) matters with foreign nations. Likewise, and again related to the points already made, the U.S. system is highly "legalistic", often involving the courts. This necessitates a greater degree of precision in the articulation of rules which citizens or government agencies must follow. Such articulation of rules can reduce the effectiveness of a U.S. negotiator, by "tipping his hand" to his opposing negotiating partners, and by limiting the scope of his bargaining possibilities.

The United States government, including Congress as well as the Executive Branch, necessarily must give some attention to the way the United States government is organized to carry out its responsibilities for protecting long term and short term United States international trade interests so that the United States can preserve some of the desirable features of its governmental system, while minimizing their otherwise damaging impact on its conduct of international affairs. Indeed, this is an added reason why the United States must also give more attention to the structure of the <u>international</u> system for international trade.

It would be dangerous indeed to view the MTN process as a job finished, to see the dispersal of experienced talent, and to hope that the new complex, intricate, and ambiguous tangle of international rules which has come out of the MTN could now be put on the shelf, like a wound up clock, to operate by itself. It will take great skill and resources, both within

the U.S. government and at the international level, to keep these MTN results from becoming merely another addition to the useless debris left strewn on the international landscape, such as the unfortunate 1948 ITO charter, the stillborn 1955 Organization for Trade Cooperation, the Kennedy Round Grains agreement, and the Kennedy Round American Selling Price agreement.