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A Primer on Issues in International Trade

"International Trade Involves the Purchase, Sale or Exchange (Barter Transactions) of Goods and Services Across National Borders"

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1. Introduction: Some Definitional Considerations

As an important part of an understanding of international trade, some definitions might be in order. The *capital account* is an account that records transactions involving the purchase or sale of tangible assets. The *current account* is the account that records transactions involving the import and export of goods and services, income receipts on assets abroad, and income payments on foreign assets inside the country. The *merchandise account* includes imports and exports of tangible goods. The *services account* includes exports and imports of services such as tourism, consulting, and banking and financial services.

The *current account surplus* occurs when a country exports more goods and services than it imports. This situation results in what is traditionally termed as a *trade surplus*. A *current account deficit* occurs when a country imports more than it exports, traditionally termed a *trade deficit*.

These definitions lay a foundation for some of the core aspects of international trade.

The Context

2009 was anything but a banner year for international or global trade—or for the international economy.[1] The World Bank reported that the volume of international trade actually fell by 14.4 percent. Bernard Hoekman, Director of the World Bank's trade group, reported that the dismal showing in international trade reflected the general position of the world economy which experienced a "distinct slowdown" in the pace of expected recovery towards the end of 2009. In fact, preliminary figures for November 2009 indicated an expansion of world trade by a paltry 1.1 percent, less than the small increase recorded for October of 1.4 percent, and far less than the encouraging 5.4 percent rise in September 2009.

The *Economist* explained that the expected resurgence in international trade may have literally fizzled because the growth in the third quarter of 2009 had been artificially buoyed by the rebuilding of business inventories, which had been slashed during the most desperate period of the world economic crisis experienced in 2009.

A second explanation may be found in exploring the sources of global demand, which has come mainly from developing and emerging markets. In fact, the ten countries whose foreign sales grew fastest in the three month period to October 2009 were all developing and emerging markets—including several Eastern European nations, plus Indonesia, and South Africa. The fastest growing representative developed nation was Australia, which exported nearly a quarter of its products to China and India. On the other side of the equation, none of the ten countries whose imports grew most rapidly

[1] Trade data in the introduction has been adapted from "Fading trading," *The Economist*, Jan. 30, 2010, p. 85.

were emerging markets. China leads the pack—perhaps somewhat artificially as a result of its program of stimulus spending.

China's share of world imports has grown from around 10 percent at the mid-point of 2008 to over 12 percent in 2009. Germany's exports grew by a healthy 3.3 percent in the three month period to September 2009. Demand in China has also boosted exports from Japan which grew by 12.1 percent in the year to December 2009. China has recently replaced America as Japan's biggest market.

Many of the decidedly negative consequences of the international economy may be alleviated by an expected rise in GDP for developed countries by 2.1% in 2010 and 2.4% in 2011. Overall, the world economy is expected to grow by a respectable 3.9% in 2010. How the renewed growth in the international economy will impact on international trade is yet to be determined.

While international trade is in itself a very important component of international economic growth and development, it certainly plays an integral role in terms of its impact on foreign direct investment or FDI. The confluence of international trade and investment is striking.

The intersection of international trade and foreign direct investment may also be reflected in the precipitous drop in the flows of foreign direct investment by 39% in 2009 to just over $1.7 trillion in 2008. The UN Conference on Trade and Development reported that all kinds of investment—equity capital, reinvested earnings, and intra company loans—were greatly affected by the economic downturn experienced in 2009. Rich or "develop" countries saw FDI inflows drop by 41%. FDI into developing countries fell by more than one-third. Professor George Yipp notes that among the most important ways a host government negatively impacts the process of globalization and FDI inflows are in fact some of the core issues involving international trade. He lists them as import tariffs and quotas, nontariff barriers, export subsidies, local content requirements, currency and capital flow restrictions, ownership restrictions, and requirements on technology transfers.[2]

This introduction to international trade is designed to assist the reader to gain an overall picture of international trade as it has developed since World War II. Topical coverage includes a discussion of the post-War War II trading system known as the GATT, the creation of the WTO in 1995, mechanisms created for settling trade disputes, and a brief introduction into two major areas of contention—dumping and illegal subsidization.

2. The Global Trading System: A Brief Overview and History

The global trading system is fraught with many pitfalls and dangers.[3] The following are some of the main barriers to free trade; many of the examples are taken from Chinese trade practices:[4]

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[2] George S. Yip, *Total Global Strategy II* (2003), p. 50.

[3] The GATT system is comprised of specific country groups, organized by region:
North America: Canada, United States of America, and territories in North America.
Latin America: Antigua and Barbuda, Argentina, Bahamas, Barbados, Belize, Bolivia, Brazil, Chile, Colombia, Costa Rica, Cuba, Dominica, Dominican Republic, Ecuador, El Salvador, Grenada, Guatemala, Guyana, Haiti, Honduras, Jamaica, Mexico, Netherlands Antilles, Nicaragua, Panama, Paraguay, Peru, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Suriname, Trinidad and Tobago, Uruguay, Venezuela and other countries and territories in Latin America.
Western Europe: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Iceland, Ireland, Italy, Liechtenstein, Luxembourg, Malta, Netherlands, Norway, Portugal, Spain, Sweden, Switzerland, Turkey, United Kingdom, Bosnia and Herzegovina, Croatia, former Yugoslav Republic of Macedonia, Slovenia, Yugoslavia (the last five countries mentioned comprise the former Yugoslavia), and territories in Western Europe.
Central and Eastern Europe, the Baltic States and the Commonwealth of Independent States (transition economies), of which *Central and Eastern Europe*: Albania, Bulgaria, Czech Republic, Hungary, Poland, Romania and the Slovak Republic; *the Baltic States*: Estonia, Latvia and Lithuania; and *the Commonwealth of Independent States (CIS)*: Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, Kyrgyz Republic, Republic of Moldova, Russian Federation, Tajikistan, Turkmenistan, Ukraine and Uzbekistan. The grouping *former USSR* refers to the Baltic States and the CIS.
Africa, of which *North Africa*: Algeria, Egypt, Libyan Arab Jamahiriya, Morocco and Tunisia; and *Sub-Saharan Africa* comprising: *Western Africa*: Benin, Burkina Faso, Cape Verde, Côte d'Ivoire, Gambia, Ghana, Guinea, Guinea-Bissau, Liberia, Mali, Mauritania, Niger, Nigeria, Senegal, Sierra Leone and Togo; *Central Africa*: Burundi, Cameroon, Central

a. High tariffs;
b. Pervasive non-tariff barriers (quotas, licenses, registration requirements, "buy local" legislation, restrictive technical, labeling,[5] and sanitary standards, and embargoes);
c. Restrictive trading rights;
d. Restrictive distribution rights;
e. Investment restrictions;
f. Voluntary export restraints.[6]

The General Agreement on Tariffs and Trade (GATT) was a multilateral treaty that was formed in 1947 by 23 nations. GATT came into force in January 1948. At that time, these 23 countries accounted for 80% of the world's trade. Recall that Western Europe was still struggling to recover from the ravages of World War II; Japan was under the authority of the United States; and colonialism reigned supreme in many nations of Africa, South-East Asia, and other parts of the world. GATT negotiations were conducted in what were termed eight separate "*Rounds*." The purpose of the GATT was to promote free trade by reducing both tariff and non-tariff barriers to international trade.[7] The GATT was devised to be a temporary regime—yet it lasted for nearly 50 years before it was replaced by the WTO in 1995.

GATT Rounds

A trade round involves a cycle of multilateral trade negotiations conducted under the authority of GATT, normally culminating in simultaneous trade agreements among participating countries to reduce tariff and non-tariff barriers to trade. Eight separate "Rounds" have been completed thus far: Geneva, 1947-48; Annecy, France, 1949; Torquay, England, 1950-51; Geneva, 1956; Geneva, 1960-62 (the Dillon Round); Geneva, 1963-67 (the Kennedy Round); Geneva, 1973-79 (the Tokyo Round); and Geneva, 1986-1993 (the "Uruguay Round").[8] There is a current series of negotiations, the "Doha Round," that have been marked by sharp disagreement between developing and developed nations. The most important of the negotiations conducted under the aegis of the GATT have included:

Dillon Round: The trade negotiations that took place from 1960 to 1962 were named after C. Douglas Dillon, then the U.S. under secretary of state, who had publicly proposed the negotiations. This Round involved 45 countries and about 4,400 tariff concessions covering $4.9 billion of trade.

African Republic, Chad, Congo, Democratic Republic of the Congo, Equatorial Guinea, Gabon, Rwanda, and Sao Tome and Principe; *Eastern Africa*: Comoros, Djibouti, Eritrea, Ethiopia, Kenya, Madagascar, Mauritius, Seychelles, Somalia, Sudan, United Republic of Tanzania and Uganda; and *Southern Africa:* Angola, Botswana, Lesotho, Malawi, Mozambique, Namibia, South Africa, Swaziland, Zambia, Zimbabwe and territories in Africa.
The Middle East: Bahrain, Cyprus, Iraq, Islamic Republic of Iran, Israel, Jordan, Kuwait, Lebanon, Oman, Qatar, Saudi Arabia, Syrian Arab Republic, United Arab Emirates, Yemen and other countries and territories in the Middle East.
Asia, of which *West Asia*: Afghanistan, Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan and Sri Lanka; and *East Asia (including Oceania)*: Australia; Brunei Darussalam; Cambodia; China; Fiji; Hong Kong Special Administrative Region of China (Hong Kong, China); Indonesia; Japan; Kiribati; Lao People's Democratic Republic; Macau, China; Malaysia; Mongolia; Myanmar; New Zealand; Papua New Guinea; Philippines; Republic of Korea; Samoa; Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu (Taipei, Chinese); Singapore; Solomon Islands; Thailand; Tonga; Tuvalu; Vanuatu; Viet Nam and other countries and territories in Asia and the Pacific.

[4] For a discussion of the various concerns raised over China's international trade regime, see Raj Bhala, "The Development of the GATT-WTO," in *International Trade Law: Theory and Practice* (2d ed., 2000), pp. 154-155. Professor Bhala provides a comprehensive review of Chinese accession negotiations to the WTO on pp. 155-183.

[5] For example, designers like Ferragamo, Gucci, and Versace are required to include the phrase "*Made in China*" on the label of garments that contain silk from China. *See* Blaise J. Bergiel & Erich B. Bergiel, "Country-of-Origin as a Surrogate Indicator" Implications/Strategies," *Global Competitiveness*, Vol. 7 (1999), p. 187.

[6] For a comprehensive list of trade barriers, see Mark Magnier, "Blockades to Food Exports Hide Behind Invisible Shields," *The Journal of Commerce*, Vol. 18 (1999), p. 5A.

[7] *See generally* Department of the Treasury, "Harmonized Trade Schedule of the United States Code of Federal Regulations No. 19, Customs Duties, Importing into the United States" (1991).

[8] John Daniels, Lee H. Radebaugh & Daniel Sullivan, "Theories and Institutions: Trade and Investment," in *International Business* (2007), p. 270. *See also* Robert Gilpin, *The Political Economy of International Relations* (1987), p. 192.

Kennedy Round: This is popular name for the sixth and at that time the most ambitious Round of trade negotiations. The Kennedy Round, which lasted from 1963 to 1967, produced concrete agreements reducing prevailing tariff levels maintained by developed countries on industrial products by about one-third, produced an historic *Antidumping Code*,[9] and a rather short-lived International Wheat Agreement which was intended to stabilize world wheat prices—an agreement which was subsequently withdrawn and never implemented. The Kennedy Round involved 48 countries and $40 billion in international trade.[10]

Tokyo Round: The Tokyo Round of multilateral trade negotiations was formally initiated by the 1973 Tokyo Declaration. It was by far the most comprehensive effort up to that time to eliminate, reduce or control some of the most pervasive non-tariff barriers that restricted non-agricultural trade. The Tokyo Round was especially important because it negotiated several codes of conduct designed to curtail the use of non-tariff barriers as instruments of trade protection. The Tokyo Round resulted in the *Tokyo Round Antidumping Code*. Like its predecessor, the Tokyo Round Antidumping Code contained rules and procedures concerning the content of antidumping regulations. An important feature of the 1979 Code was a requirement that antidumping investigations be reported, and a semi-annual report on cases be submitted to the GATT Secretariat. More countries (102) participated in these negotiations than in any previous Round. The Round involved $300 billion in trade. Most notably, more than 20 developing countries that were not GATT members and several countries of Eastern Europe with very different economic systems were active participants. The Tokyo Round was carried out in Geneva and concluded there in 1979.[11]

Uruguay Round: The Uruguay Round, concluded in Geneva in December 1993, was the latest series of concluded multilateral trade negotiations aimed at revising, updating and expanding the coverage of the GATT. The Uruguay Round was formally launched in September 1986 at the GATT Ministerial in Punta del Este, Uruguay. The negotiations concentrated once again on the elimination of tariff and non-tariff barriers to trade and on the development of clear, transparent, and enforceable international trading rules. The provisions of the Uruguay Round agreement especially considered the unique perspective of developing countries struggling to establish regimes of international trade. The final agreement accorded more time to developing countries than to industrialized countries in order to come into compliance with trading rules. The category of least developed countries (LDCs) were accorded even more time or exempted altogether from some of the provisions of the agreement.[12] The Uruguay Round involved 118 countries and $3.7 trillion in trade.

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[9] As result, during the Kennedy Round, the GATT Antidumping Code of 1967 was established. Its three main functions were: (1) to clarify and elaborate on the broad concepts found in Article VI of the GATT; (2) to supplement Article VI by establishing appropriate procedural requirements for antidumping investigations; and (3) to bring all GATT signatory countries into conformity with Article VI. *See* House Committee on Ways and Means, 104th Cong., 1st Sess., *Overview and Compilation of U.S. Trade Statutes* (June 25, 1997), p. 66.

[10] *See* Kenneth W. Dam, *The GATT* (1970), pp. 68-73, 76-77.

[11] *See* Kenneth W. Dam, *The GATT* (1970), pp. 72-73; Robert Gilpin, *The Political Economy of International Trade Relations* (1987), pp. 196-197.

[12] Least-developed countries include: Afghanistan, Angola, Bangladesh, Benin, Bhutan, Burkina Faso, Burundi, Cambodia, Cape Verde, Central African Republic, Chad, Comoros, Democratic Republic of the Congo, Djibouti, Equatorial Guinea, Eritrea, Ethiopia, Gambia, Guinea, Guinea-Bissau, Haiti, Kiribati, Lao People's Democratic Republic, Lesotho, Liberia, Madagascar, Malawi, Maldives, Mali, Mauritania, Mozambique, Myanmar, Nepal, Niger, Rwanda, Samoa, Sao Tome and Principe, Senegal, Sierra Leone, Solomon Islands, Somalia, Sudan, Togo, Tuvalu, Uganda, United Republic of Tanzania, Vanuatu, Yemen and Zambia.

The following are the main points of the Uruguay Round agreement:

- **Tariffs**: GATT member countries agreed to cut their import tariffs by a 36-percent average.
- **Textiles**: Countries agreed to end the 20-year-old system of import quotas on textiles and apparel by 2005; tariff quotas would be converted into tariffs, which would then be subjected to further reductions over time.
- **Agriculture**: Countries agreed to scale back direct export subsidies by 36 percent below rates in place between 1986 and 1990, by 2001; countries also agreed to reduce the quantity of subsidized commodities exported. They also agreed to convert quotas, import licenses, and other import limits into tariffs that would be gradually reduced.
- **Services**: For the first time, countries agreed to create basic rules so that services providers were afforded the same treatment in host countries as in their home markets.
- **Intellectual Property**: As an important concession to developed countries, negotiators agreed to protect and enforce patent rights, trademarks, and copyrights, and to limit the trade of counterfeited creative works and inventions. Article 3 of the TRIPS Agreement[13] mandates national treatment for intellectual property protection. Article 4 creates a "Most Favored Nation" obligation for such protection.[14]
- **Investments**: Concerning foreign direct investment or FDI, countries agreed to eliminate investment measures that limit or force certain types of investments, for example, the "golden share"; to offer full "national treatment" to foreign investors; and to eliminate quotas on investments and other financial restraints.
- **Subsidies**: Countries agreed to create rules concerning the legality of subsidies by defining three classes of subsidization: *prohibited, actionable, and non-actionable subsidies.*
- **Dumping**: Countries agreed to create more detailed rules governing the ability of GATT members to take action against the importation of a product sold at an unfairly discounted export price, i.e., to attack the problem known as "dumping."
- **Safeguards**: Countries agreed to strengthen rules concerning "temporary import limits" created to protect domestic industries from surges of fairly-traded imports (i.e., safeguards). Members agreed not to maintain safeguard protections for more than eight years, and to prohibit "gray area measures"—in essence, voluntary export restraints and other informal agreements to curtail fairly traded imports.
- **Institutional Structure**: Perhaps most importantly, members agreed to create a **World Trade Organization**, which would be a permanent international organization representing all of the major economic classifications of nations (developed, developing, least developed), that would replace the GATT with a stronger, permanent institution.
- **Dispute Resolution**: The GATT was not originally intended to be an international organization, but was rather intended to be a *traditional multilateral treaty* designed to function under the *International Trade Organization* (ITO). However, the ITO never came into being. It would be fair to conclude that by default, the GATT became the governing body for settling international trade disputes. There was one major problem: the GATT had no independent enforcement mechanism. It had to rely on "moral suasion," or the good will of member countries. The GATT achieved major progress in increasing the nature and volume of world trade. In the interim period, members agreed

[13] The TRIPS Agreement is Annex 1C of the Marrakesh Agreement Establishing the World Trade Organization, signed in Marrakesh, Morocco on 15 April 1994.

[14] *See* House of Representatives [Uruguay Round Trade Agreement], *Statement of Administrative Action, Agreement on Trade-Related Aspects of Intellectual Property Rights*, H.R. Doc. No. 316, 103d Cong., 2d Sess., Vol. 1 (Sept. 27, 1994), pp. 981-990.

to strengthen GATT's dispute resolution rules by allowing countries to block findings by GATT expert panels, but only if all members opposed the finding.[15]

Doha Round

The Doha Development Round or Doha Development Agenda (DDA) is the current trade-negotiation round under the authority of the World Trade Organization (WTO), which commenced in November 2001. As of 2010, talks remained stalled over a divide on several issues including agriculture, industrial tariffs, non-tariff barriers, services, and trade remedies. The most significant differences lie between developed nations led by the European Union (EU), the United States, and Japan and the major developing countries represented mainly by India, Brazil, China, and South Africa. Considerable contention also existed between the EU and the United States over the United States' maintenance of agricultural subsidies—seen to operate effectively as a trade barrier against agricultural imports from the European Union.

The Doha Round began with a ministerial-level meeting in Doha, Qatar in 2001. Subsequent ministerial meetings took place in Cancún, Mexico (2003),[16] and Hong Kong (2005). Related negotiations took place in Geneva, Switzerland (2004, 2006, 2008); Paris, France (2005); and Potsdam, Germany (2007).

The July 23-29, 2008 negotiations in Geneva broke down after failing to reach a compromise on agricultural import rules. Brazil, Mexico and an alliance of developing nations—known as the "Group of 22"—had walked out of the negotiations when the EU and Japan attempted to turn the focus of negotiations to international investment rules and antitrust policies without first taking on the issue of farm-subsidy programs. Nevertheless, intense negotiations—most notably between the USA, China, and India— were held at the end of 2008 in order to agree on a protocol for further negotiations. Leading economic powers (the G-8, plus China, India, Brazil, Mexico, and South Africa) pledged to reach an accord by 2010. Time will tell if this timetable is realistic.

3. The World Trade Organization (WTO)

The **WTO** was created on January 1, 1995 to be the primary international organization regulating all matters of international trade.[17] The WTO was also designed to administer international investment accords. The WTO currently has more than 150 members and accounts for more than *97 percent of world trade*. Around 30 other countries, including perhaps most importantly the Russian Federation, are engaged in negotiations to become full members of the WTO. Specifically, the WTO was created in order to meet the following policy objectives:

- Assist in the free flow of trade by reducing both tariff and non-tariff barriers;
- Negotiate further openings in world markets;
- Implement, administer, and carry out the various WTO Agreements; and
- Settle trade disputes between members.

Specifically, the WTO will meet its objectives by:

1. Providing market access to the products of other WTO members by lowering import tariffs on both industrial and agricultural goods;

[15] A 1994 Congressional act established the relationship between the Uruguay Round agreements and U.S. law. *See* House of Representatives [Uruguay Round Trade Agreement], *Statement of Administrative Action, Agreement Establishing the World Trade Organization*, H.R. Doc. No. 316, 103d Cong., 2d Sess., Vol. 1 (Sept. 27, 1994), pp. 669-678.

[16] Following Cancun, the WTO determined that U.S. cotton subsidies were illegal. In subsequent negotiations, the United States agreed to cut farm subsidies for such crops as cotton, corn, rice, wheat and soybeans by 20%. Elizabeth Becker, "U.S. Will Cut Farm Subsidies in Trade Deal," *The New York Times* (on line), July 31, 2004, at http://www.nytimes.com/2004/07/31/business/worldbusiness/31geneva.html.

[17] *See* WTO, "An Introduction to the WTO," http://www.wto.org.

2. In keeping with the philosophy of the GATT, encouraging trade with all member nations on a non-discriminatory basis;
3. Opening up service markets to foreign competition;
4. Providing effective intellectual property protection;
5. Instituting policies for attracting FDI;
6. Ensuring "transparency" in trading regimens by requiring the "listing" of all tariffs imposed;
7. Ensuring uniform application of trade policies; and
8. Placing restrictions on state-owned-enterprises (SOE's), in order to remove favorable national treatment and discrimination against foreign entities and foreign competition.

The foundation of the WTO is a concept called *normal trade relations*. This means that, in effect, a member of the WTO must extend the same favorable terms of trade (formerly called the "Most Favored Nations" Rule) to *all members* of the WTO that they unilaterally extend to any *one* member. The scope of the MFN principle includes customs duties and charges of any kind imposed on or in connection with the importation, exportation, and international transfer of payments for imports and exports; the method of levying such duties and charges; all rules and other formalities in connection with importation and exportation; and matters which cover internal taxes and regulatory laws.[18] Note that MFN rules applied only to products.

The actual text providing for MFN/normal trade relation status reads:

"Any advantage, favor, privilege or immunity granted by any member 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 other members."

The web site of the WTO may be found at www.wto.org.

There are two major exceptions under the WTO:

1. Developing countries' manufactured products may be given preferential treatment over those from industrial (developed) countries.[19]
2. Concessions granted to members within a regional trading alliance, such as the EU or NAFTA,[20] may be granted but may not been extended generally to countries outside of the trade alliance.

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[18] *See* Edwin I. Barber, "Investment-Trade Nexus," in *U.S. International Economic Policy* (Gary Clyde Hufbauer, ed.) (The International Law Institute, 1982), p. 12.

[19] The concept of a *Generalized System of Preferences* (GSP) was first introduced in the United Nations Conference on Trade and Development (UNCTAD) in 1964 for developing countries (LDCs). Through tariff preferences in developed countries, the LDCs claimed they would be able to increase their exports and foreign trade earnings that would be vital to economic transformation. Section 502 of the Trade Act of 1974 authorizes the President to designate a country or a territory as a *Beneficiary Developing Country* or BCD. The President was prohibited from designating any country for GSP benefits based on specific criteria. However, the President may waive certain conditions if he determines and reports to the Congress reasons that the designation of a particular country is in the "national economic interest." The exclusionary criteria included:

- In certain cases, the country is a communist country;
- Is a party to an arrangement that causes a serious disruption to the world economy;
- Affords "reverse preferences" to other developed countries which have or are likely to have a significant adverse effect on U.S. commerce;
- Has nationalized or expropriated U.S. property, unless "adequate and effective" compensation has been paid, negotiations are underway to provide such compensation, or a dispute over compensation is in arbitration;
- Fails to recognize as binding or to enforce arbitral awards in favor of the U.S.;
- Aids or abets by granting sanctuary from prosecution to any individual or group which has committed international terrorism; or
- Has not taken or is not taking steps to afford internationally recognized workers' rights to its domestic workers, as defined by 19 U.S.C. § 2467(4).

See generally House Committee on Ways and Means, 105th Cong., 1st Sess., *Overview and Compilation of U.S. Trade Statutes* (Comm. Print, June 25, 1997), pp. 12-19.

4. Dispute Settlement and the WTO: An Overview

Dispute settlement is a major component of the WTO—one that was lacking under the GATT, which contained no effective enforcement procedures. How does dispute settlement fit into the general organization of the WTO?[21]

The highest level of decision-making in the WTO is the *Ministerial Conference* which meets at least once every two years. The next level is the *General Council*, composed of ambassadors and the director of a country delegation, which meets on a regular basis. The General Council also meets as the *Trade Policy Review Body* and the *Dispute Settlement Body*. The next level includes the *Council for Trade in Goods*, the *Council for Trade in Services*, and the *Council for Trade-Related Intellectual Property Rights* (TRIPS). The WTO also includes several important "working groups" that deal with individual agreements and other areas such as the environment, development, membership applications, and regional trade agreements.

Under the WTO, trade agreements are considered essentially as *enforceable contracts*. The following represents the manner in which a dispute may be settled in procedures before the WTO:

First stage: consultation or negotiations (up to **60 days**). If an informal process fails, the parties can request the WTO director-general to mediate or try to help in any other manner.

Second stage: Upon a failure of consultations or negotiations, an "expert" panel of 3-5 individuals is constituted (up to **45 days** for a panel to be appointed, plus 6 months for the panel to conclude). The country whose policy is being challenged can block the creation of a panel once, but when the Dispute Settlement Body meets for a second time, the appointment of a panel can no longer be blocked—unless there is a consensus against appointing the panel.

Officially, the panel is serves as a resource for the Dispute Settlement Body. However, the report of the panel can only be rejected by consensus in the Dispute Settlement Body. As a practical matter, its conclusions are difficult to overturn. The panel's findings must be based on the agreements cited.

The panel's final report should normally be given to the parties to the dispute within six months. The WTO notes, however, that in cases of urgency, including those concerning perishable goods, the deadline may be shortened to three months.

Panel Procedures

Each side in the dispute presents its case in writing to the panel before the first hearing. At the first hearing, the case for the complaining country and defense are heard. In addition, parties who have announced they have an "interest in the dispute" may be permitted to make their case. After the first

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[20] NAFTA, which includes Canada, Mexico, and the United States, came into effect in 1994. NAFTA is an example of a free trade agreement (FTA) whose main goal is to abolish all tariffs between member countries. NAFTA also may be distinguished from a customs union which is a grouping of countries which agree to levy a common external tariff on goods imported from nonmembers. NAFTA covers the following subject areas:

- *Market access*, involving tariff and nontariff barriers, rules of origin, and government procurement;
- *Trade rules*, involving safeguards, subsidies, countervailing and antidumping duties, health and safety standards;
- *Services*, providing for the same safeguards for trade in services that exist for traditional trade in goods;
- *Investment*, establishing investment rules governing minority interests (the "golden share"), portfolio or traditional investments, real property, and majority-owned or controlled investments from NAFTA countries; in addition, NAFTA coverage would be extended to investments made by any company incorporated in NAFTA country, regardless of country of origin;
- *Intellectual property*, relating to creation, protection, and enforcement of intellectual property rights;
- *Dispute settlement*, providing for a process that will be followed by signatory countries, designed to keep countries from undertaking unilateral actions against an offending party.

See Linda M. Aguilar, "NAFTA: A Review of the Issues," *Economic Perspectives* (Federal Reserve Bank of Chicago, 1992), p. 14.

[21] Adapted from WTO, Dispute Settlement, http://www.wto.org/english/tratop_e/dispu_e/dispu_e.htm.

hearing, the countries involved submit written rebuttals and present oral arguments. If one side to the dispute raises scientific or other technical matters, the panel may consult experts or appoint an expert review group to prepare an advisory report.

First draft: The panel submits the descriptive (factual and argument) sections of its report to the two sides to the dispute. Each side is accorded two weeks to comment. The first draft does not include findings and conclusions. Next, the panel submits an *interim report* to the two sides, including its findings and conclusions, giving the parties one week to ask for a review. The period of review must not exceed two weeks. During that time, the panel may hold additional meetings with the two sides in order to resolve the dispute. A *final report* is submitted to the two sides and three weeks later, it is circulated to all WTO members. If the panel concludes that the disputed trade measure or practice is in violation of a WTO agreement or obligation, it recommends that the measure or practice be made to conform to WTO rules. The panel may suggest a methodology for compliance which may include the imposition of *fines* or perhaps *trade sanctions*.

The report becomes the Dispute Settlement Body's ruling or recommendation within 60 days unless a consensus rejects it. Both sides can appeal the report.

The Appeal

Appeals have to be based on points of law. As in the American legal system, an appeal cannot seek to reexamine existing evidence or raise issues not raised in earlier procedures. An appeal is heard by three members of a permanent seven-member Appellate Body set up by the Dispute Settlement Body. This Appellate Body represents the broad range of WTO membership. Members of the Appellate Body serve a four-year term. Members of the Appellate Body are individuals with "recognized standing in the field of law and international trade," and should not be affiliated with any government.

The appeal can *uphold, modify, or reverse* the panel's legal findings and conclusions. Normally, the appellate process should not exceed 60 days, with an absolute maximum of 90 days. The Dispute Settlement Body is required to accept or reject the appeals report within 30 days. A rejection is only possible by consensus.

- Two issues have been especially vexing: dumping and subsidization.

5. Issues of Dumping and Subsidies: An Introduction

Professor Raj Bhala suggests that "tariffs no longer matter in international trade law." He notes that in the period 1947 (when GATT entered into force) and 1994 (the eve of the entry into force of the Uruguay Round), average tariffs in industrial countries plunged from 40 percent to 6.3 percent. As a result of the Uruguay Round, the average tariff will fall to 3.9 percent and the percentage of industrial products receiving duty-free treatment will rise from 20 to 43 percent. Professor Bhala pivots from a traditional analysis and continues, "Non tariff barriers are what matters in late 20th and early 21st century international trade law."[22] As a consequence, two of the major complaints regularly raised in international trade negotiations are those of *dumping* and granting of unfair or illegal *subsidies* by a nation to a domestic industry.

Dumping

It is clear that export pricing is a very difficult process. The exporter must be careful to take into account unique export-related costs and include them in the final price quotation of goods. These costs are in addition to the normal costs shared with the domestic side. As noted by *Czinkota, Ronkainen, Moffett and Moynihan*, these special export (risk) considerations generally include:

- The cost of *modifying* the goods for foreign markets;

[22] Raj Bhala, "Rethinking Antidumping Law," *George Washington Journal of International Law and Economics*, Vol. 29 (1995), pp. 3-6, 8-23, in Raj Bhala, *International Trade Law: Theory and Practice* (2d ed., 2000), pp. 830-839.

- *Operational costs* of the export operation. Examples cited are personnel, market research, additional shipping and insurance costs, communication costs with foreign customers, and overseas promotional costs.
- Costs incurred in *entering or penetrating* foreign markets. These costs include tariffs and import taxes; commercial credit risks and political risks associated with a buyer in a foreign market; and costs dealing in another than the exporter's domestic currency—foreign exchange risk.[23]

What happens when domestic production is challenged by less expensive imports? A question arises: Might some of these imports arrive in the domestic market as a result of foreign competition designed to *unfairly compete* with domestically produced goods? In more specific terms, have goods been literally dumped into the domestic market?

First, a legal definition is in order. Dumping is defined as the practice of exporting a product at a price lower than the price that the product normally or regularly commands in the domestic market or at a price lower than its actual cost to produce. There are significant accounting implications in any analysis of dumping because of special considerations associated with the practice of *transfer or intracompany pricing*—the practice of pricing sales to members of a corporate family.

The difference between the price in the foreign market/cost of production and the price in the U.S. market is called the *dumping margin.*

In the United States, a domestic producer may petition the government to impose *antidumping duties* on any imports alleged to have been dumped in the American market. In order to qualify, proof must indicate:

- Predatory (intentional) and not merely unintentional dumping is actually occurring;
- The U.S. government can calculate "with reasonable specificity" the damage to its own companies; and
- The American government can show that the damage is significant (generally the petitioners must represent at least 25% of domestic production in any given industry.)

Because dumping is essentially an act by an individual company and not an act of a country, the WTO cannot punish a country in which the company accused of dumping is based. However, the situation may be quite different in a country that is organized under the model of central planning where the factors of production are owned or tightly controlled by the state. China, Viet Nam, Cambodia, Cuba and other economies similarly organized immediately come to mind.

If a company has engaged in dumping, it is incumbent upon the nation in which the company is located to take action against that company. If a nation fails to remedy the situation after proof of dumping has been made, the aggrieved country may legally impose an *antidumping duty on the product—in essence, it may place an additional tariff* on the imported product.

The number of antidumping cases indicates that dumping is indeed a real world problem but is an area that is fraught with definitional and proof problems.

Subsidies

The subsidies agreement negotiated under the Tokyo Round begins by defining a subsidy. Article 1 requires two elements: (1) a "financial contribution by a government or any public body" within that government territory, and (2) consequent conferral of "a benefit."[24] If a government believes that its products are suffering from unfair competition due to official government subsidies that a nation is "paying" or "allowing" to a domestic producer which *causes or threatens to cause serious prejudice to its interests*, a nation may "retaliate" against such a product by charging a *countervailing duty to offset*

[23] *See generally*, Michael R. Czinkota, Ilkka A. Ronkainen, Michael H. Moffett & Eugene O. Moynihan, *Global Business* (2001), p. 440.

[24] *See* House of Representatives [Uruguay Round Trade Agreement], *Statement of Administrative Action, Agreement on Subsidies and Countervailing Measures*, H.R. Doc. No. 316, 103d Cong., 2d Sess., Vol. 1 (Sept. 27, 1994), pp. 911-923.

the subsidy—in effect, an *additional tariff* placed on an imported product that has been receiving the unfair subsidy. These decisions are reviewable by the WTO.

Examples of subsidies may include the following: direct transfers of funds through grants or loans; assistance to a company through loan guarantees; foregoing of revenues through tax credits; or other price or income supports that target a specific enterprise or industry, specific groups of enterprises or industries, or enterprises in a particular sector or region. It appears that all nations engage in some form of subsidization or export promotion as a part of national economic policy. This area is fraught with political implications and a lack of precision in definition and scope of coverage.

Articles 3-9 of the Agreement establish a three-tiered framework for categorizing subsidies and subsidy remedies: (1) subsidies that are prohibited under all circumstances (the "Red Light" category); (2) subsidies that may be challenged in a WTO dispute settlement procedure and domestically countervailed if they cause adverse trade effects (the "Yellow Light" or "Dark Amber" subsidies); and (3) subsidies that are non-actionable and non-countervailable if they are structured according to criteria intended to limit their potential for causing trade distortions (the "Green Light" category").

In the United States, an industry, a manufacturer, or a trade union may file a petition with the *Import Administration and the United States International Trade Commission* (ITC) that will then conduct an investigation of the matter. Each country provides its own "list" of parties who may file a complaint. Antidumping duties and countervailing duties as trade remedies have been successfully pursued by a variety of domestic industries including producers of steel, industrial equipment, computer chips, agricultural products, textiles, chemicals, and consumer products. These twin issues will continue in importance in the future.

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