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## From Diplomacy to Law: The Juridicization of International Trade Relations

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# From Diplomacy to Law: The Juridicization of International Trade Relations

*Dr. Arie Reich\**

## I. INTRODUCTION

### A. Presentation of the Thesis

This article deals with the development of law; i.e., the evolution of a legal regime in a field which prior thereto was not subject to law. It is my view that such a process took place in recent decades in the area of trade relations between sovereign nations. The period since World War II, and particularly recent years, is marked by the clear development of a conventional legal regime which regulates trade relations among the majority of countries of the world, as expressed by the multiplication of legal norms and the strengthening of the binding nature of these norms and the procedures for enforcing them. An in-depth examination of this phenomenon and an analysis of its political and economic causes may shed light on not only an important phenomenon in the field of international law, but also on the role of law generally in human society.

An international trade agreement will always be in the nature of a compromise by each of the State Parties between each State's aspiration to attain the economic benefits introduced by the agreement,

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and each State's desire to preserve optimum sovereignty. On the one hand, every international agreement naturally contains limitations on the freedom of action of each State and constrains the policy options open to it. On the other hand, the economic benefits which each State wishes to attain through the trade agreement, will not be achieved in their entirety unless there is reciprocal honouring of the obligations contained in the agreement. The first consideration, the preservation of sovereignty and prevention of restrictions on courses of action, creates a tendency towards preferring non-binding agreements and agreements which leave the optimum freedom of action to the State, for example, by flexible or vague drafting, and use of "escape clauses" and weak enforcement procedures. Such agreements allow flexibility in honoring obligations and retain scope for diplomatic manoeuvring. This will allow the States to consider internal political interests which may arise in the future and which may require measures to be taken that are contrary to their commitments under the agreement. Such scope of action is, of course, open to exploitation by all parties. The more it is exploited, the greater is the uncertainty in international commerce. The greater the uncertainty, the more severe is the injury to the other parties to the Agreement. The greater the severity of injury, the higher are the chances that the economic goals of the agreement will be frustrated.

In this constant conflict between opposing interests, in the past, the political scales tipped in favor of sovereignty and flexibility. The trade agreements, to the extent they existed, were limited in their contents and were less binding in their nature. Many governments saw these agreements not as a binding legal regime but as a DIPLOMATIC-POLITICAL framework which could provide a "basis for negotiation between States for the purpose of attaining a balance between benefits and obligations."<sup>1</sup> In recent years, however, there is a growing demand by States to regulate their trade relations by using norms and enforcement procedures that are LEGAL in character, create significant limitations on the sovereignty of the States, and, in extreme cases, even exclude the States' power to determine policy in certain socio-economic fields. The most prominent examples of this latter

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<sup>1</sup> These statements were made in the past in relation to the GATT agreement. Cf. OLIVIER LONG, LAW AND ITS LIMITATIONS IN THE GATT MULTILATERAL TRADE SYSTEM 21 (1985). In the 1970s, Long was the Secretary General of GATT. He states: "These limitations reflect the difficulties inherent in any attempt to regulate within a legal framework something as dynamic and fluctuating as world trade, despite provisions for waivers, exceptions and a safeguard clause." See generally KENNETH W. DAM, THE GATT: LAW AND INTERNATIONAL ECONOMIC ORGANIZATION 335-36 (1970); and in greater detail, see *infra* Part II, para.C:1.

phenomenon are provided by the treaties establishing the European Community (EC).<sup>2</sup> In other international frameworks, a similar trend is also apparent, even if it does not possess the extreme characteristics of the EC. This process is hereinafter termed the "juridicization process"<sup>3</sup> of international trade relations, a term which is meant to encompass developments both on the substantive and procedural level.

The writings in this field have hitherto concentrated on the institutional developments, particularly in connection with the new dispute settlement procedures of the World Trade Organization (WTO).<sup>4</sup> In this context, commentators have spoken of "judicialization" of the General Agreement on Tariffs and Trade (GATT), a term that refers to the "judiciary," i.e., the mechanism entrusted with resolving disputes and ruling on questions of interpretation. This thesis, in contrast, argues for a more integrated perspective on the developments in the international trade arena—a perspective that views law as a general phenomenon composed of both substantive and institutional components and one that is not confined to the multilateral level alone. In our view, the procedural and institutional developments in the WTO form a specific part of a more general trend of world-wide proportions, which is reflected in significant developments both of the substantive law of international trade relations and of its institutional setting in the multilateral GATT agreements and in regional and bilateral trade arrangements. What we have here is a process of legal evolution, where a new international legal regime regulating the trade policies of governments is gradually evolving.

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<sup>2</sup> See, for example, the statements of the European Court in the famous case *Costa v. ENEL*, E.C.R. 585. 593 (1964): "By creating a Community of unlimited duration, having its own institutions, its own personality, its own legal capacity and capacity of representation on the international plane and, more particularly, real powers stemming from a limitation of sovereignty or a transfer of powers from the States to the Community, the Member States have limited their sovereign rights, albeit within limited fields, and have thus created a body of law which binds both their nationals and themselves."

<sup>3</sup> "Juridicization" deriving from the word "*Juridicus*", which means of, or pertaining to, courts or a legal system, and which also hints at the term "*Jure Gentium*", "the law of nations". The term "legalization", which some modern commentators use is less appropriate, as it pertains to the process of making something lawful; in other words, making lawful a phenomenon which prior thereto was against the law, a meaning which of course is not applicable to this discussion. Another important distinction, which will be used later, is between "rule oriented" and "power oriented" relationships. See JOHN H. JACKSON, *THE WORLD TRADING SYSTEM: LAW AND POLICY OF INTERNATIONAL ECONOMIC RELATIONS* 85 (1991).

<sup>4</sup> See, e.g., Ernst-Ulrich Petersmann, *The Dispute Settlement System of the World Trade Organization and the Evolution of the GATT Dispute Settlement System Since 1948*, 31 *COMMON MKT. L. REV.* 1157 (1994); ROBERT HUDEC, *ENFORCING INTERNATIONAL TRADE LAW: THE EVOLUTION OF THE MODERN GATT LEGAL SYSTEM* (1991).

In order to prove this claim, Part II of this article examines the evolution of the multilateral regime governing international trade relations known as GATT, over the last fifty years until the establishment of the WTO. Its transformation from a primarily diplomatic framework for coordination of trade policies to a legal regime imposing welfare-enhancing limitations on government intervention in the economy is described and analyzed. To illustrate the juridicization process in bilateral trade arrangements, Part III then examines developments in the international trade agreements of Israel, the author's home country. The various stages of development in these agreements—concluded with most of the major trading powers—also demonstrate very clearly an identical trend of juridicization as found on the multilateral level. In Part IV, I then attempt to offer explanations to the phenomenon by analyzing its economic and political roots, using some of the theories and models developed within the discipline of international relations.<sup>5</sup> Finally, I shall attempt to tie the process of juridicization to the phenomenon of law as a whole and to what is known about the stages and causes of the development of law in human society.

#### B. Methodology: Defining the Criteria for Examining the Phenomenon

Prior to turning to a review of developments in this field, it is necessary to attempt to define the standards according to which the phenomenon will be examined. More specifically, according to which criteria will a particular arrangement be regarded as more "legal" than another?

Legal scholars generally, and researchers in international law in particular, have conducted extensive discussions about the proper definition of the term "law,"<sup>6</sup> and it has even been suggested (even if somewhat exaggerated) that the number of definitions of law is as many as the number of lawyers.<sup>7</sup> For purposes of this article, I shall use the definition proposed by Professor Yoram Dinstein, a prominent Israeli scholar of International Law. Professor Dinstein defines law as "a binding normative arrangement which a society establishes in order

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<sup>5</sup> See *infra* Part D. On the use of this discipline to understand international law, see generally Kenneth W. Abbott, *Modern International Relations Theory: A Prospectus for International Lawyers*, 14 YALE J. INT'L L. 335 (1989); Anne-Marie Slaughter Burley, *International Law and International Relations Theory: A Dual Agenda*, 87 AM. J. INT'L L. 205 (1993).

<sup>6</sup> See, e.g., Glanville L. Williams, *International Law and the Controversy Concerning the Word "Law"*, 22 BRIT. Y.B. INT'L L. 146 (1945).

<sup>7</sup> YORAM DINSTEIN, *INTERNATIONAL LAW AND THE STATE* 14 (1971).

to limit human behaviour.”<sup>8</sup> The characteristics which therefore identify the “legal” nature of any system, as already emphasized by Aquinas,<sup>9</sup> are their “binding” character and their power to “limit” the behavior of persons acting within their framework.<sup>10</sup> Accordingly, international arrangement “A” is deemed to be more “legal” than international arrangement “B,” if and to the extent that arrangement “A” creates more severe limitations on the behavior of States than does arrangement “B.” This effect may occur because of the profusion of norms in arrangement “A,” the stricter formulation of the provisions in arrangement “A,” or the efficacy of the enforcement procedures in

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<sup>8</sup> *Id.* In accordance with this approach, Prof. Dinstein thereafter defines international law as “a binding normative arrangement which international society establishes in order to limit human behaviour.” *Id.* at 26. Similar definitions have been offered by other prominent scholars of international law. Brierly’s classical definition of international law refers to “the body of rules and principles of action which are binding upon civilized states in their relations with one another.” J. BRIERLY, *THE LAW OF NATIONS* 1 (H. Waldock 6th ed., 1963). The term “binding” implies both the mandatory character of international legal norms, as well as their restrictive impact on the states who are subject to them. See also J.G. Starke’s definition of a legal norm, *infra* note 10.

A contending definition would be that of John Austin, who defined law as the “command of the sovereign,” and who regarded the existence of sanctions in case of disobedience as a crucial element of any legal system. See JOHN AUSTIN, *THE PROVINCE OF JURISPRUDENCE DETERMINED* 12 (London: Weidenfeld & Nicolson, 1968). This approach, which is strongly influenced by Austin’s perception of municipal legal systems—in particular the English one—has been widely criticized and cannot be employed in the field of public international law. See G. Williams, *International Law and the Controversy concerning the Word “Law,”* 22 BRIT. Y.B. INT’L LAW 146, 147-48 (1945). Indeed, Austin did not regard international law as “law, properly so called,” but as “positive morality.” *Id.* If experience has shown us that “almost all nations observe almost all principles of international law and almost all of their obligations almost all of the time”—as Louis Henkin has put it—that, in my mind, proves the inaccuracy of Austin’s definition of “law,” rather than the non-existence of international law. See LOUIS HENKIN, *HOW NATIONS BEHAVE: LAW AND FOREIGN POLICY* 47 (2d ed. 1979).

<sup>9</sup> Thomas Aquinas (1224-1274) in *Summa Theologica*, defines the nature of law as follows: “Law is a rule or a measure of action in virtue of which one is led to perform certain actions and restrained from the performance of others. The term “law” derives [etymologically] from “binding”, because by it one is bound to a certain course of action.” THOMAS AQUINAS, *SUMMA THEOLOGICA* Qu. 90 (J.G. Dawson trans.), quoted in LORD LLOYD OF HAMPSHIRE & M.D.A. FREEMAN, *LLOYD’S INTRODUCTION TO JURISPRUDENCE* 151 (5th ed. 1985).

<sup>10</sup> The definition of the term “law” in the Oxford Dictionary, emphasizes these characteristics:

“a rule enacted or customary in a community and recognized as enjoining or prohibiting certain actions and enforced by the imposition of penalties.” CONCISE OXFORD DICTIONARY 670 (1990).

This definition also explains that the enforcement of legal rules is exercised by means of sanctions and not by force, a stipulation which conforms with norms of public international trade law.

The definition of a legal norm is also given by the renowned scholar of international law, J.G. Starke: “A norm. . . is a prescription enjoining a defined mode of action.” J.G. Starke, *Monism and Dualism in the Theory of International Law*, 17 BRIT. Y.B. INT’L L. 66 (1936).

arrangement "A." In all three cases, the result is that courses of action which were previously available to the State are now constricted, and certain actions may no longer be performed legitimately within the framework of the arrangement.<sup>11</sup>

### C. The Politics and Economics of International Trade Agreements

Although every international trade agreement has its own specific background anchored in the prevailing specific political and economic interests of the States involved, there are some general characteristics common to all trade agreements which may explain the need for these agreements and their similar content.

The primary purpose of the trade agreements considered below is the dismantling of barriers to international trade. These barriers are found in different forms; tariffs and import charges, bureaucratic obstacles to imports, and subsidies are only a partial list of the various possibilities. Common to all of these forms of barriers is that they originate in government policy, the purpose or result of which is the protection of local industry against competition by foreign manufacturers.<sup>12</sup> Some of the agreements also deal with trade barriers which do not originate in government interventionism but, rather, in anti-competition activities of private corporations.<sup>13</sup>

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<sup>11</sup> The following is an illustration: if John Doe promises to give Richard Roe £100 "when I want to", no legal obligation is created, as his "promise" does not restrain him in any way whatsoever. Everything depends on his will, and so long he does not "want" to give the money—he is under no obligation to do so. Similarly, a State's undertaking not to place protective tariffs on certain products—where this undertaking is subject to the right of the State to claim the existence of various "special circumstances," or the existence of a situation where it has almost unqualified discretion to accept the complaint of a local manufacturer about imports being dumped, and to impose a levy on the said imports—is much less "legal" than where such reservations do not exist.

<sup>12</sup> It is customary to divide trade barriers into two categories: custom tariffs (i.e., customs duties and charges equivalent to customs duties), and non-tariff barriers (NTBs). The latter category includes an almost endless list of methods of distorting the flow of trade, a list which is as extensive as the inventive powers of government officials around the world. They also include export incentives which aid local manufacturers to compete with foreign manufacturers in export markets. A GATT Secretariat report prepared in the 1970s lists more than 600 non-tariff barriers. See *Quantitative Restrictions and Other Non-Tariff Barriers*, Nov. 30, 1984, GATT B.I.S.D. (31st Supp.) at 211 (1985). A list prepared by the United Nations Conference on Trade and Development in the 1980s reached a much higher number, see UNCTAD, *Non-Tariff Barriers Affecting the Trade of Developing Countries and Transparency in World Trading Conditions: The Inventory of Non-Tariff Barriers* (Geneva: UNCTAD, 1983).

<sup>13</sup> See Treaty Establishing the European Economic Community, Mar. 25, 1957, arts. 85-86, 298 U.N.T.S. 11, 47-49 (1957); Convention Establishing the European Free Trade Association, Jan. 4, 1960, art. 15, 370 U.N.T.S. 3, 15-16 (1960) [hereinafter EFTA]; Agreement Between the European Economic Community and the State of Israel, May 11, 1975, 1975 O.J. (L 136) 3. Generally, these provisions prohibit anti-competition activities, such as co-ordination of prices,

At the root of the trade agreements lies what is termed the liberal economic doctrine,<sup>14</sup> which aims to reduce government intervention in the flow of trade between States, while recognizing that free trade is beneficial to the economies of all the acceding States. This doctrine originates in the theories of renowned economists of the 18<sup>th</sup> and 19<sup>th</sup> centuries, led by David Hume,<sup>15</sup> Adam Smith,<sup>16</sup> David Ricardo,<sup>17</sup> and John Stuart Mill.<sup>18</sup> According to the "Theory of Relative Advantage," proposed by Ricardo,<sup>19</sup> a State will always prefer to specialize in industrial sectors in which it has a relative advantage (in comparison with other industrial sectors) and permit free trade with foreign countries in the remaining sectors with the aim of importing those products which it needs in return for the fruits of its most efficient labor. Such an economic arrangement will lead to reciprocal benefits for all the participating States. Every obstacle which prevents this beneficial trade is detrimental to all the participating States, not only to the State which wished to export, but also to the State which was to gain from the import. This theory is, therefore, a refinement of the concept of specialization, referred to by Plato<sup>20</sup> and developed by Smith and Ricardo. Ricardo's theory is still highly regarded by economists<sup>21</sup> and provides a powerful intellectual underpinning for the policy of free

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establishment of cartels, and exploitation of dominant positions of monopolies, in so far as such activities impair trade between the countries involved.

<sup>14</sup> MICHAEL J. TREBILCOCK & ROBERT HOWSE, *THE REGULATION OF INTERNATIONAL TRADE* 20 (1995).

<sup>15</sup> In 1752, David Hume was the first to repudiate the claims of the mercantile economists of the 17<sup>th</sup> and 18<sup>th</sup> centuries, according to which governments should aim to limit imports and maximize exports with the purpose of increasing gold reserves. He showed the existence of a mechanism which always tends to equalize the international balance of payments of States. Hume's mechanism is described by Paul A. Samuelson. PAUL A. SAMUELSON, *THE THEORY OF ECONOMICS* 648 (M. Eto trans.) (3d ed. 1963).

<sup>16</sup> ADAM SMITH, *AN INQUIRY INTO THE NATURE AND CAUSES OF THE WEALTH OF NATIONS* bk. IV, ch. II (1890) (1723-1790).

<sup>17</sup> DAVID RICARDO, *THE PRINCIPLES OF POLITICAL ECONOMY AND TAXATION* 77 (1911) (1772-1823).

<sup>18</sup> JOHN STUART MILL, *PRINCIPLES OF POLITICAL ECONOMY* (1848) (1806-1873).

<sup>19</sup> RICARDO, *supra* note 17.

<sup>20</sup> See PLATO, *THE REPUBLIC* (Francis MacDonald Cornford trans., Oxford University Press 1941). Plato uses the idea of specialization and the division of labour in order to explain the origins of human society: "So the conclusion is that more things will be produced and the work be more easily and better done, when every man is set free from all other occupations to do, at the right time, the one thing for which he is naturally fit. . . We shall need more than four citizens, then to supply all those necessities we mentioned, For the farmer, naturally, will not make his own plough. . ." *Id.* at bk. 2, 71-73. Thereafter, Plato also draws the inevitable conclusion, *i.e.*, the indispensability of international trade, at least for the purpose of supplying products which are not manufactured in that State. *Id.*

<sup>21</sup> TREBILCOCK & HOWSE, *supra* note 14, at 2-3.



trade which is at the basis of international trade agreements. As the modern economist Paul Samuelson, winner of the Nobel Prize for Economics, phrased it: "In fact, the supporters of free trade have one reason only, but this reason is of pre-eminent weight: free trade promotes a mutually beneficial division of labour among nations, greatly increases the chance of growth in real national product, and enables a higher standard of living world-wide."<sup>22</sup>

However, based on this rationale, States ought to adopt a *unilateral* policy of free trade, as England chose to do in the second half of the 19<sup>th</sup> century while relying on the theories of Smith and Ricardo<sup>23</sup> and without need for recourse to international agreements. The theory of free trade is unable to explain the necessity for reciprocity which underlies international trade agreements and characterizes most of the liberalization achieved in recent decades in international trade.<sup>24</sup> Accordingly, commentators,<sup>25</sup> while applying the Public Choice Theory, generally point to internal political failures which lead to a flawed decision-making process in which too much weight is given to the concentrated interests of protected industries, i.e., their owners and workers, at the expense of the thinly spread interests of consumers who are forced to bear the costs of protection.<sup>26</sup> This situation is created by the superior organizational and lobbying power of the protected industries in comparison to the large consumer public, whose individual *per capita* interests are much smaller than those of the members of the protected industries. As a result, it is very difficult to politically break down trade barriers unless compensation is offered to industry in the form of new foreign markets. These markets can be opened up to them as a result of international trade agreements that

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<sup>22</sup> SAMUELSON, *supra* note 15.

<sup>23</sup> See G. CURZON, *MULTILATERAL COMMERCIAL DIPLOMACY: GATT AND ITS IMPACT ON NATIONAL COMMERCIAL POLICIES AND TECHNIQUE* ch. I (1965); *see also* SHEPARD B. CLOUGH & CHARLES W. COLE, *ECONOMIC HISTORY OF EUROPE* 473 (1941).

<sup>24</sup> Most of the liberalization was achieved through the GATT agreement, which is discussed below, and through regional agreements, such as the European Community, EFTA, and bilateral free trade areas. Examples of unilateral liberalization are sparse and are exceptions to the rule; one is the "Program to Expose the Economy to Imports from Third Countries." *See Israeli Finance and Industry Ministers Agree to Dismantle Trade Barriers over Seven Years*, 8 Int'l. Trade Rep. (BNA) 395 (Mar. 13, 1991) [hereinafter *Dismantle Trade Barriers*].

<sup>25</sup> ARTHUR DOWNS, *AN ECONOMIC THEORY OF DEMOCRACY* (1957); MANCUR OLSON, *THE LOGIC OF COLLECTIVE ACTION* (1965); Charles K. Rowley & Robert D. Tollison, *Rent Seeking and Trade Protection*, in *THE POLITICAL ECONOMY OF RENT SEEKING* 217 (Charles K. Rowley et al. eds., 1988).

<sup>26</sup> For an extensive discussion of the politics of trade protection and the various economic models which have been developed to explain the political process in this connection, see MICHAEL J. TREBILCOCK ET AL., *TRADE AND TRANSITIONS: A COMPARATIVE ANALYSIS OF ADJUSTMENT POLICIES* 171-92 (1990).

are based on reciprocal, as opposed to unilateral, liberalization. Moreover, in this connection, every government is affected by the "prisoners' dilemma" arising out of the desire to dismantle barriers in export-markets in addition to liberalization at home.<sup>27</sup> If it disbands its barriers unilaterally, it will not have the wherewithal to "pay" its partners for removing their barriers as well.<sup>28</sup>

Since the signing of the English-French trade agreement in 1860 (Cobden-Chevalier Treaty), it has been clear to modern statesmen that international trade agreements may be an extremely useful tool for liberalization in trade (an idea which was not easily accepted by the supporters of unilateral free trade policy in England).<sup>29</sup> These agreements in fact create an international system of regulation whose purpose is to deal with national systems of regulation; the latter restrict trade and protect local industry against foreign competition, whereas the former aspire to eliminate restrictions, promote trade, and expose industry to international competition. The international agreements also aim in this way to reduce uncertainty and instability existing in international trade, where every State is completely free to take measures against, and impose restrictions on, exports of other countries.<sup>30</sup> The international trade agreements therefore implement the vision of the UN Charter to "employ international machinery for the promotion of the economic and social advancement of all peoples."<sup>31</sup> Using the terminology of the New Haven School approach

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<sup>27</sup> The dilemma is created because every State is likely to prefer preserving its own trade barriers, while anticipating a unilateral lowering of barriers on the part of the other State on the basis of that country's own internal interests. Thus, the State which "holds out" longest will ultimately succeed in opening its export markets without needing to open its own markets for imports. When both countries adopt this policy, ultimately, both loose. In this situation, it becomes worthwhile for each country to aim for co-operation in the form of an international agreement for reciprocal liberalization. See Robert Axelrod & Robert O. Keohane, *Achieving Cooperation Under Anarchy*, in CO-OPERATION UNDER ANARCHY 226 (Kenneth A. Oye ed., 1985); see also William R. Cline, "Reciprocity": A New Approach to World Trade Policy?, in TRADE POLICY IN THE 1980s 121, 152 (William R. Cline ed., 1983).

<sup>28</sup> This is one of the reasons that the State of Israel, even within the framework of the Unilateral Exposure Program, retained customs at minimal levels and did not cancel them altogether, i.e., so as to enable "payment" in future negotiations with third countries. See *Dismantle Trade Barriers*, *supra* note 24. See also H.C.J. 1452/93 *Igloo v. Minister of Trade and Industry* 47(5) P.D.610, para. 5 of the judgment, where it was held by Israel's High Court of Justice that the requirement of reciprocity in international trade is a legitimate consideration on the part of the authorities, which justifies refusing an import permit.

<sup>29</sup> For a comprehensive historical overview, see GILBERT R. WINHAM, THE EVOLUTION OF INTERNATIONAL TRADE AGREEMENTS 15-20 (1992).

<sup>30</sup> See *id.* at 12; Cf. ROBERT O. KEOHANE, AFTER HEGEMONY 87-88 (1984).

<sup>31</sup> U.N. CHARTER Preamble.

to international law,<sup>32</sup> international trade agreements act on the level of attaining "optimal order," and not only "minimal order," in the international community by maximizing the allocation of economic resources.

## II. THE PROCESS OF JURIDICIZATION OF THE GATT REGIME

### A. Historical Background of the GATT

Today, the GATT forms the most important multilateral framework for the regulation and coordination of the international trade policies of most of the countries of the world. The conception and birth of this agreement were inspired by the vision of "a new order" in the world economy based on cooperation and liberal principles and was led by the heads of Western States at the end of World War II.<sup>33</sup> The basic rules for this new order were laid down by an international economic conference, which took place in July 1944 in Bretton Woods, with the intention of structuring it around three international organizations—the International Monetary Fund (IMF), the World Bank (IBRD) and the International Trade Organization (ITO). The ITO was intended to operate as a permanent institution which would both promote the reciprocal removal of barriers and provide a forum for enforcing obligations in this connection and resolving disputes.<sup>34</sup>

From 1946 to 1948 delegations from tens of countries labored over the preparation of a constitution for this organization. The constitution was finally signed in Havana in 1948 by 53 States.<sup>35</sup> Concurrently, an ancillary agreement was drafted which provided for the substantive rules of trade, stating what was permitted and prohibited and to what extent each country undertook to reduce its tariffs. This agreement was called the General Agreement on Tariffs and Trade, or GATT.<sup>36</sup> However, when the ITO Convention (known as the Havana Charter) was presented for ratification to the United States Congress, it was met by the vehement opposition of members of the Senate. They saw it as a serious threat to the sovereign power of the United States (as well as to the powers of Congress) to determine trade policy and economic policy as the United States saw fit without some inter-

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<sup>32</sup> See LUNG-CHU CHEN, AN INTRODUCTION TO CONTEMPORARY INTERNATIONAL LAW 85-87 (1989).

<sup>33</sup> See ANDREAS F. LOWENFELD, INTERNATIONAL ECONOMIC LAW, VOL. VI, PUBLIC CONTROLS ON INTERNATIONAL TRADE 15-16 (2d ed. 1983).

<sup>34</sup> *Id.* at 16.

<sup>35</sup> *Id.* at 20.

<sup>36</sup> General Agreement on Tariffs and Trade, *opened for signature* on October 30, 1947, 55 U.N.T.S. 194; T.I.A.S. No. 1700 [hereinafter GATT].

national body deciding for it what was to be allowed and what was to be forbidden.<sup>37</sup> When other countries in the world saw that the ITO would not be ratified by the U.S. Congress, they too refused to ratify it and, thus, the fate of the ITO was sealed. However, the GATT, which had been signed in November 1947, came into force by virtue of a Protocol of Provisional Application.<sup>38</sup> It began life without the institutional umbrella of the ITO and almost without administrative, supervisory or enforcement procedures, but primarily with substantive rules.

The absence of this institutional framework has been felt strongly over the years, and there is no doubt that it has impaired the effectiveness of the substantive rules. Despite this, the demands of reality led to the creation of some inferior substitutes to the institutions and procedures which were missing.<sup>39</sup> Attempts made over the years to revive the ITO or other types of legal enforcement procedures were always met by opposition from numerous governments and so failed.<sup>40</sup> Only recently, in the last round of talks conducted within the GATT framework (the Uruguay Round) between 1986-1994,<sup>41</sup> half a century after the Bretton Woods Conference, was the historical circle completed and the necessary international agreement obtained to establish the WTO. This organization aims to provide the institutional framework for the substantive rules contained in the GATT agreements, rules which in the meantime have grown and expanded immeasurably.<sup>42</sup> Towards the end of 1994, the U.S. Congress ratified the new agreement creating the WTO, although it possessed characteristics similar

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<sup>37</sup> Cf. LOWENFELD, *supra* note 33, at 20; William Diebold, *The End of the I.T.O.*, PRINCETON ESSAYS IN INTERNATIONAL FINANCE, No. 16 (1952).

<sup>38</sup> See GATT, *supra* note 36.

<sup>39</sup> Thus, for example, even though there is no reference in the GATT agreement to any organizational structure, it is stated therein that decision in connection with the agreement will be made by "the parties acting together", and not by any organization or body (see Article XXV). This provision formed the basis for the *de facto* establishment of the "GATT Council" which gathered at least once every six months to make decisions and settle trade disputes. In the beginning GATT also had no secretariat and this problem too was resolved by a fiction; after the Havana conference a temporary commission was set up to establish the international trade organization (ICITO) (which in fact was never established), and the secretariat of this commission in practice served the needs of GATT. For details, see JACKSON, *supra* note 3, at 37-38.

<sup>40</sup> *Id.* at 38.

<sup>41</sup> For a detailed historical review of the measures taken in the Uruguay Round, see JOHN CROOME, *RESHAPING THE WORLD TRADING SYSTEM: A HISTORY OF THE URUGUAY ROUND* (Geneva: World Trade Organization, 1995).

<sup>42</sup> Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations, Agreement Establishing the World Trade Organization, 33 I.L.M. 1 (1994) [hereinafter WTO Agreement].

to those of the agreement which the Congress had consistently refused to ratify since 1948.

The fifty-year history of the GATT agreement, a world regime which is undoubtedly the most important and comprehensive of all international trade agreements, provides the most prominent example of the juridicization process argued for here. I will examine developments within this agreement in greater detail.

## B. The Multiplication and Strengthening of Substantive Norms

As noted earlier, juridicization is expressed also by the multiplication and strengthening of substantive norms. Perhaps the most concrete example of this phenomenon is the fact that the GATT of 1947 has expanded from an agreement of about eighty pages to an agreement of some 26,000 pages in its most recent version signed in Marrakesh in 1994! It is not only the longest agreement in the world, but perhaps also the most important multilateral agreement since the signing of the UN Charter.<sup>43</sup> From an agreement signed by twenty-three countries, GATT has grown into an organizational framework currently uniting 124 countries and the EC,<sup>44</sup> as well as a dozen of other countries which are in the process of joining. It has been transformed from a provisional, short-term agreement<sup>45</sup> into a permanent and complex framework comprising more than 200 multilateral trade agreements.<sup>46</sup>

From the material point of view, an unmistakable process is taking place forging and spreading a system of norms which regulates the entire range of policy measures in international trade and even beyond. We shall briefly identify the main elements of this process.

### 1. *The Normative Regimes in relation to Non-Tariff Barriers (NTBs)*

The original GATT agreement, in fact, contained numerous articles intended to deal with Non-Tariff Barriers (NTBs). However, many of these articles were drafted in an overly "weak" manner, allowing States to evade them and maintain various types of barriers without being deemed to breach the agreement. Further, the Protocol

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<sup>43</sup> Cf. Petersmann, *supra* note 4, at 1160.

<sup>44</sup> CROOME, *supra* note 41.

<sup>45</sup> See GATT, *supra* note 36. The GATT agreement was brought into temporary force in 1947 by the Protocol of Provisional Application with the hope that the Havana Charter would soon be ratified, together with the ancillary GATT agreement.

<sup>46</sup> See GATT, Status of Legal Instrument, 1993 ed. (Geneva: GATT, 1993).

of Provisional Application, which gave the agreement its legal validity, was subject to a "grandfathering" provision which protected legislation already in force in the acceding countries, even if that legislation was contrary to GATT.<sup>47</sup>

Consider, for example, the issue of product-standards, which was often used as a convenient mechanism through which to implement a protectionist policy under the pretext of safeguarding consumer safety and product quality. Even though a mandatory product standard, whose principal purpose is none other than the protection of local products produced according to this standard, amounts to a "quantitative restriction" (which is expressly prohibited by Article XI of GATT), it falls within the special exception provided by subsection 2(b) of this Article, and would thus be permitted.<sup>48</sup> Only at the end of the 1970s, during the Tokyo Round, did the developed countries recognize the urgent need to deal with this serious trade barrier, and an agreement ancillary to the GATT was signed, namely "the Agreement on Technical Barriers to Trade," also known as "the Standards Code." This agreement created a new system of rules and norms in relation to the manner of creation and operation of standards with the purpose of ensuring that they would not be used as a disguised barrier to trade. However, only a minority of the GATT contracting parties, principally the industrial nations, acceded to the new code. This is also the reason why it was necessary to create a separate agreement, and it was not possible to simply add the new rules to the existing GATT. Most of the GATT parties opposed it, and it was not possible to amend the GATT without their consent.<sup>49</sup>

A similar process may be seen with regard to other NTBs, such as preferential treatment of local suppliers in government procurements, import licensing, the use of anti-dumping procedures, and the bestowment of subsidies. The original GATT provisions enabled the continued use of these trade barriers, either because the issue was not

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<sup>47</sup> See GATT, *supra* note 36. See Article 1(b) of the Protocol of Provisional Application, which applies Part II of the GATT agreement (the part which contains the provisions relating to Non-Tariff Barriers) "to the fullest extent not inconsistent with existing legislation."

<sup>48</sup> Art. XI ("General Elimination of Quantitative Restrictions"), para. 2(b) provides: "The provisions of paragraph 1 of this Article shall not extend to. . . import. . . restrictions necessary to the application of standards. . ." See GATT, *supra* note 36, art. XI(2)(b).

<sup>49</sup> According to Article XXX of the GATT, amendments to the provisions of Part I of the Agreement require the acceptance of *all* the GATT contracting parties. See GATT, *supra* note 36, art. XXX. The provisions of the rest of the Agreement can be amended by a majority of two thirds. It was usually impossible to gather even a two thirds majority, considering the fact that most of the contracting parties were developing countries, reluctant to accept the advanced liberalization sought by the industrialized parties. See JACKSON, *supra* note 3, at 51-52.

referred to at all or because the rules which were established were too flexible and insufficiently "legal" (i.e., binding). Only during the Tokyo Round, which ended in 1979, did some countries set up new and separate normative structures for the purpose of regulating these matters.

The process of juridicization in the field of norms did not end at this stage, it continued and took a large step forward during the negotiating round that ended in 1994. The progress is reflected on a number of levels:

- The spread of the normative regime to numerous other countries and, in practice, to all the parties to the GATT. This result was achieved by the transformation of the ancillary agreements from voluntary codes open to accession at will to obligatory agreements which form part of the so-called "single undertaking." Thus, it is not possible to be a member of the new GATT and the WTO without being bound by all the aforesaid agreements.<sup>50</sup> What could not be done in the 1970s, in other words, the ability to persuade the majority of GATT parties to agree to the strict rules in relation to NTBs, became feasible in 1994!
- The creation of completely new normative regimes on NTBs, for example, the Agreement on Sanitary and Phytosanitary Measures,<sup>51</sup> the Agreement on Preshipment Inspection,<sup>52</sup> the Agreement on Trade-Related Investment Measures (TRIMS),<sup>53</sup> the Agreement on Safeguards,<sup>54</sup> and more.
- The improvement and widening of existing regimes. Under this heading we would include, *inter alia*: the Agreement on Government Procurement,<sup>55</sup> the Standards Code,<sup>56</sup> the Dumping Code,<sup>57</sup> and the Subsidies Code.<sup>58</sup>

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<sup>50</sup> This is true of all the ancillary agreements mentioned here except for the Agreement on Government Procurement, which for a variety of reasons was left as a voluntary agreement (or according to the GATT terminology a "plurilateral" agreement). See Arie Reich, *The New GATT Agreement on Government Procurement: The Pitfalls of Plurilateralism and Strict Reciprocity* (forthcoming in the April 1997 issue of the JOURNAL OF WORLD TRADE).

<sup>51</sup> WTO Agreement, *supra* note 42, Annex 1A:4.

<sup>52</sup> *Id.* Annex 1A:10.

<sup>53</sup> *Id.* Annex 1A:7.

<sup>54</sup> *Id.* Annex 1A:14.

<sup>55</sup> Published in URUGUAY ROUND OF MULTILATERAL TRADE NEGOTIATIONS, 31 LEGAL INSTRUMENTS EMBODYING THE RESULTS OF THE URUGUAY ROUND (Geneva: GATT Secretariat). On the GATT Agreement on Government Procurement, see Reich, *supra* note 50.

<sup>56</sup> WTO Agreement, *supra* note 42, Annex 1A:6 (Agreement on Technical Barriers to Trade).

<sup>57</sup> *Id.* Annex 1A:8 (Agreement on Implementation of Article VI).

<sup>58</sup> *Id.* Annex 1A:13 (Agreement on Subsidies and Countervailing Measures).

## 2. *The Normative Regime in Relation to Subsidies*

Another field which amply illustrates the juridicization process, from the beginning of GATT in 1947 until today, is the international regulation of subsidies.

Subsidies, the direct or indirect benefits given to business elements by the government, may artificially influence the flow of trade and distort the efficient allocation of economic resources, both by reducing imports and by increasing exports. Article XVI of the original GATT deals with this problem using a mixture of "soft law" and "hard law," the former being the clearly dominant component. The sole duty provided in this Article which applies to *all* types of subsidies affecting trade<sup>59</sup> is the duty to give notice in writing to the GATT Council on the existence of such a subsidy, its extent, nature, and estimated level of influence on trade, and on the circumstances making the subsidization necessary. (Even this limited obligation was seldom honored by the contracting parties.) The Article provides that if it is determined that serious prejudice to the interest of any other contracting party is caused or threatened by such subsidization, "discussions" may be held between the subsidizing State and the injured State concerning "the possibility of limiting" (but not eliminating!) the subsidization. This, therefore, is a clear example of the very diplomatic and non-binding formulations generally used by the GATT.

The Article continues by concentrating on one category of subsidies — export subsidies. While the Article proclaims the Parties' recognition of the harmful effects which such subsidies may have for other contracting parties and recognizes their ability to hinder the achievements of the objectives of GATT, the Article does not introduce any operative provisions.<sup>60</sup> The picture continues to narrow in turning to a sub-category of export subsidies for "primary products,"<sup>61</sup> although here too the wording is qualified ("contracting parties shall seek to avoid. . ."). A real legal prohibition in fact only exists in relation to a very narrow band within the wide range of subsidies which distort trade. This very narrow band includes only those export subsidies within the range of primary products which result in the subsi-

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<sup>59</sup> That is, such a subsidy by one of the parties to the agreement "which operates directly or indirectly to increase exports of any product from, or to reduce imports of any product into, its territory" (from Article XVI:1).

<sup>60</sup> *Id.* art. XVI:2.

<sup>61</sup> "Primary products" are defined as "any product of farm, forest or fishery, or any mineral, in its natural form or which has undergone such processing as is customarily required to prepare it for marketing in substantial volume in international trade." See GATT, *supra* note 36, Annex I, art. XVI(B)(2) (Interpretative Note).



dizing State acquiring for itself more than "an equitable share" of world export trade in that particular product.<sup>62</sup>

In the 1970s, within the framework of the Tokyo Code, great progress was made in this field, with the establishment of the Subsidies Code which set up a system of rules which were stricter and less diplomatic than the GATT rules. Here, export subsidies for all industrial products were decisively prohibited, without requiring any further conditions to be met.<sup>63</sup> Similarly, an annex was attached to the agreement, providing an illustrative list of "export subsidies," in lieu of a comprehensive definition of this term.<sup>64</sup>

Nevertheless, there was still a wide range of subsidies which did not fall within the ambit of the list and which could not be classified as export subsidies. Some of these subsidies could potentially harm the trade of other countries and the efficient allocation of economic resources, even though they were not necessarily granted only in connection with export. The Subsidies Code of the Tokyo Round was still far from being an overall regulation of the subject. This was reflected in difficult and acrimonious controversies between the large countries regarding the definition of what was allowed or forbidden in this field and in disputes having far-reaching economic repercussions. The fate of entire industrial sectors were at stake, such as the civilian aircraft industry: the European Airbus Co., on the one hand, and the American Boeing and McDonnell Douglas companies on the other. The Americans accused the Europeans of unfair trade by awarding huge sums in subsidies to the Airbus company, a large number of whose aircrafts is exported to other countries, whereas the Europeans responded that Boeing enjoyed indirect governmental support in the form of military R&D contracts awarded by the U.S. Department of Defense. Resolving such disputes was extremely difficult in the absence of clear legal rules regarding subsidies and a binding legal mechanism for dispute settlement.

Recently, during the Uruguay Round, the GATT parties succeeded in reaching agreement on a general and comprehensive regime

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<sup>62</sup> See GATT, *supra* note 36, art. XVI(3). In relation to interpretation and application of this requirement, see French Assistance to Exports of Wheat and Wheat Flour, GATT B.I.S.D. (7th Supp.) at 46 (1958), for the decision of the Panel of 1958 on Australia's complaint against France regarding a French subsidy for the export of wheat and wheat flour.

<sup>63</sup> See Article 9 of the Agreement on Interpretation and Application of Articles VI, XVI and XXIII of the General Agreement on Tariffs and Trade, GATT B.I.S.D. (26th Supp.) at 56 (this agreement is commonly referred to as the Tokyo Round Subsidies Code).

<sup>64</sup> "Annex: Illustrative List of Export Subsidies". The Annex forms an integral part of the agreement. See Article 19:10. *Id.*

of binding definitions and rules concerning subsidies, which would bind all the members of the WTO (and not just the few countries which had previously joined the Code).<sup>65</sup> The agreement offers, for the first time, a comprehensive definition of the term "subsidy," while dividing all types of subsidies into three categories: "prohibited subsidies,"<sup>66</sup> "actionable subsidies"<sup>67</sup> (i.e., subsidies which are actionable only in certain circumstances, such as when they cause injury to another Member State<sup>68</sup>), and "non-actionable subsidies" (i.e., permitted subsidies).<sup>69</sup>

Even if the new agreement is not complete in terms of content and will require extensive interpretation and implementation, there is no doubt that it represents a big step forward when compared to the earlier agreement and is an important milestone in the process of creating a stable and comprehensive legal system in a highly problematic and sensitive area of international trade relations.

### 3. *New Regimes in Services and Intellectual Property*

Up to 1994, the GATT regime dealt solely with trade in goods. However, additional economic resources exist which may be traded, such as services and intellectual property. The agreement reached during the Uruguay Round meets this deficiency by means of two new agreements which create a normative framework to regulate these areas.

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<sup>65</sup> Agreement on Subsidies and Countervailing Measures, Annex 1A:13 of The Agreement Establishing the World Trade Organization, *reprinted in THE RESULTS OF THE URUGUAY ROUND OF MULTILATERAL TRADE NEGOTIATIONS: THE LEGAL TEXTS* 1-46 (1994).

<sup>66</sup> *Id.* This category contains two principal types:

- A. Subsidies, as defined in Article 1, contingent, in law or in fact, whether solely or as one of several other conditions, upon export performance, including those set out in the Illustrative List of Annex 1;
- B. Subsidies which are contingent as aforesaid upon the use of domestic over imported goods.

<sup>67</sup> *Id.* pt. III.

<sup>68</sup> *Id.* art. 5. This category refers to all types of subsidies, including those which are not export incentives. The article prohibits use of such a subsidy if it has "adverse effects" on the interests of other States, such as injury to the domestic industry of another Member, or "nullification or impairment of benefits" accruing directly or indirectly to other Members under GATT 1994. For the interpretation of the above term, which has been a key term in GATT dispute settlement since its inception, *see infra* Part II, para. 3.1.

<sup>69</sup> *Id.* pt. IV. This category includes subsidies which are not "specific" within the definition of the agreement, as well as subsidies awarded to assist research and development (subject to certain limitations), to assist disadvantaged regions, and to provide assistance to promote adaptation of existing facilities to new environmental requirements, which result in greater constraints and financial burdens on firms.

The General Agreement on Trade in Services (GATS)<sup>70</sup> is the first step towards regulating the trade sector possessing the highest rate of growth in the developed countries, with the purpose of attaining gradual liberalization of this sector in the international arena. The agreement is built on principles which are very similar to those of GATT on goods.<sup>71</sup> It also adopts the gradual approach of GATT, employing protracted negotiations for the opening of selected service sectors to international competition on the basis of reciprocity.<sup>72</sup> Under this approach, every State is obliged to grant "national treatment" to the other GATT Member States in those service sectors which it has agreed to open as aforesaid.<sup>73</sup> Similarly, every State is bound to the principle of "transparency," which requires it to publish all the statutes, regulations, and administrative guidelines regulating the right to supply services within its territory, and supply all the necessary information in this regard.<sup>74</sup> In this way, every foreign supplier of services (such as banks, insurance companies, communications companies, architects, or lawyers) will be able to know its rights and obligations, and it will be possible to maintain surveillance on the parties' implementation of their commitments. As noted, the agreement is only a first step in the process of liberalizing this area, but it will clearly become the future arena for the continuation of the juridicization process.

The Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs)<sup>75</sup> also regulates a field of major importance in the modern economy. The agreement provides appropriate standards and rules for the protection and exploitation of intellectual property rights, such as patents, copyrights, trademarks, industrial designs, ge-

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<sup>70</sup> WTO Agreement, *supra* note 42, Annex 1B [hereafter GATS Agreement].

<sup>71</sup> Compare GATS Agreement, *supra* note 70, art. II (Most-Favoured Nation Treatment), art. XIV (General Exceptions), and art. XVII (National Treatment) with GATT, *supra* note 36, art. I, art. XX, and art. III, respectively.

<sup>72</sup> See GATS Agreement, *supra* note 70, art. XIX.

<sup>73</sup> See *id.* art. XVII.

<sup>74</sup> See *id.* art. III.

<sup>75</sup> General Agreement on Tariffs and Trade - Multilateral Negotiation (the Uruguay Round), *Agreement on Trade-Related Aspects of Intellectual Property Rights, Including Trade and Counterfeit Goods*, Dec. 15, 1993, arts. 22-24, 33 I.L.M. 81, 91-93 (1994) [hereinafter TRIPs Agreement]. For discussions on the TRIPs Agreement, see generally, Jasna Arsic, *Combating Trade in Counterfeit Goods - The GATT and the EC Approaches*, 18 WORLD COMPETITION LAW & ECON. REV. 75 (Mar. 1995); Paul E. Geller, *Intellectual Property in the Global Marketplace: Impact of TRIPs Dispute Settlements*, 29 INT'L LAW. 99 (1995); J.H. Reichman, *Universal Minimum Standards of Intellectual Property Protection Under the TRIPs Component of the WTO Agreement*, 29 INT'L LAW. 345 (1995). For a discussion on the influence of TRIPs on the developing countries, see Marco C.E.J. Bronckers, *The Impact of TRIPs: Intellectual Property Protection in the Developing Countries*, 31 COMMON MKT. L. REV. 1245 (1994).

ographical indications, trade secret and integrated circuits.<sup>76</sup> The agreement was signed on the backdrop of widespread infringements, particularly in the Far East, of intellectual property rights of Western manufacturers, and the emergence of a huge counterfeiting industry, which, in the opinion of many economists, seriously impairs the profitability of investments in research and development of new inventions and creations. The agreement is intended to ensure appropriate protection for these intellectual property rights by means of binding internal legislation in all GATT States. *Inter alia*, the Member States are obliged to ensure the existence of legal enforcement procedures to enable effective action against infringement of intellectual property rights.<sup>77</sup> Similarly, they are obliged to enable judicial review of all administrative decisions relating to intellectual property rights.<sup>78</sup>

In this field, a number of international conventions have in fact been in existence for many years.<sup>79</sup> However, these agreements lacked the strong enforcement mechanism of the WTO and were, therefore, powerless in dealing with infringements.<sup>80</sup> Similarly, many developing countries, which had preferred not to accede to these conventions in order not to harm their local industry, could now no longer afford not to become members of the WTO.

### C. The Evolution of GATT's Enforcement Mechanism

The juridicization process of trade relations is probably most clearly reflected in the enforcement and dispute settlement mechanism of GATT. The reason for this is evident; the ability to enforce a norm or to impose a sanction for failure to obey it, is what largely distinguishes "soft law" from "hard law." In the context of international trade, the clash between the sovereignty of the State and the international norm will be most apparent and publicly visible. On one side will be the State's particular national interest (at least as perceived by its government); on the other side will be the global economic interest in the success of the international regime.

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<sup>76</sup> Uruguay Round Trade Agreement Draft Implementation Proposal, June 29, 1994, at B(16), available in LEXIS Intlaw Library, GATT File.

<sup>77</sup> See TRIPs Agreement, *supra* note 75, art. 41(1).

<sup>78</sup> *Id.* art. 41(4).

<sup>79</sup> For example, the Paris Convention for the Protection of Industrial Property was last amended in 1967, and the Berne Convention for the Protection of Literary and Artistic Works was last amended in 1971.

<sup>80</sup> Lars-Henrik Knutrud, *TRIPs in the Uruguay Round*, in *THE NEW WORLD TRADING SYSTEM: READINGS* 193 (1994).

1. *Dispute Settlement in GATT up to 1994*

As noted above, the Havana Charter, with its review and dispute settlement mechanisms, was rejected by the political organs of the States, chief among them the U.S. Congress. Left in GATT itself was a fairly feeble mechanism, primarily found in Article XXIII. Indeed, many countries preferred a flexible and non-legalistic framework such as this for settling trade disputes, in light of the political sensitivity of such disputes and the need to preserve the sovereignty of the States.<sup>81</sup> In their view, dispute settlement within the GATT framework had to be based on consultations, negotiations and diplomatic compromises.

The cause of action required to activate a dispute settlement procedure in GATT is not a "breach" of the agreement (as is the case in most agreements) but, rather, a somewhat vague term unique to GATT — "nullification or impairment of benefits."<sup>82</sup> The term has been interpreted as referring to the situation where the actions of one State harm the trade of another State, thereby impairing the benefits which the latter State was reasonably entitled to expect when negotiating its obligations under the agreement.<sup>83</sup> The use of this term again reflects the flight from legal categories and the preference for economic-diplomatic categories. These latter categories prefer the substantive-concrete approach, which is directed towards the protected commercial interest, over the formalistic-legal approach. Whereas the term "breach" confers importance on the written word, the GATT term places emphasis on the reasonable economic expectations of the parties to the agreement and on the principle of reciprocity<sup>84</sup> which

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<sup>81</sup> See, e.g., R. Phan van Phi, *A European View of the GATT*, 14 INT'L BUS. LAW. 150 (1986); Lisa S. Klainman, *Applying GATT Dispute Settlement Procedures to a Trade in Services Agreement: Proceed with Caution*, 11 U. PA. J. INT'L BUS. L. 657 (1990). See also DAM, *supra* note 1, at 356 (referring to the general recognition in the 1960s among the GATT contracting parties that "legalism does not contribute to trade liberalization," in international trade in connection with the dispute settlement mechanism).

<sup>82</sup> GATT, *supra* note 36, art. XXIII. This term is both wider and more limited than the term "breach." The term is more limited because it is necessary to prove impairment of the benefits accruing to the complainant under the Agreement. A breach on its own, without any injury, is insufficient. The term is wider because it is possible to have such impairments without any formal breach of the provisions of GATT, and this will give rise to a right of complaint under the Agreement.

<sup>83</sup> Australian Subsidy on Ammonium Sulphate, Apr. 3, 1950, GATT B.I.S.D. (Vol. 2) at 188, 192-93 (1952). See also Treatment by Germany of Imports of Sardines, Oct. 31, 1952, GATT B.I.S.D. (1st Supp.) at 53, 58-59 (1953).

<sup>84</sup> The principle of reciprocity is central to GATT as demonstrated by its preamble: "Being desirous of contributing to these objectives by entering into reciprocal and mutually advantageous arrangements. . ." GATT, *supra* note 36, preamble. GATT also states that in certain types of negotiations and agreements, the contracting parties "shall endeavour to maintain a general level of reciprocal and mutually advantageous concessions. . ." *Id.* art. XXVIII.

underlies it. It is also likely that the GATT approach reflects a general skepticism in relation to the capacity of legal formulations to close all the possible loopholes. Consequently, it also favors the ability to complain of violations which do not comprise a formal breach of the provisions of the agreement.<sup>85</sup>

According to GATT, disputes between two States in relation to the agreement may first be subjected to diplomatic consultations between the parties to the dispute.<sup>86</sup> In this framework, any complaining State presents a written complaint to the other concerned State or States.<sup>87</sup> The latter State is obliged to agree to the complaining State's request for consultations and examine its claims in good faith with the aim of finding an agreed solution which will be to the satisfaction of both parties.<sup>88</sup> In the event that such a solution is not found, power is given to the CONTRACTING PARTIES, i.e., the GATT Council, to investigate the matter and make "appropriate recommendations" to the parties involved.<sup>89</sup> If the State causing the injury, which often has been found to be in breach of its commitments under GATT, refuses to accept the recommendations, the GATT Council may then authorize the injured party to suspend the application to the injuring party of such concessions or obligations under GATT "as they determine to be appropriate in the circumstances."<sup>90</sup> In other words, the injured State will in such case be authorized to take retaliatory measures against the injuring State by way of non-fulfilment of certain obligations towards it, for example, through raising tariffs on certain products of that country or other similar measures.

However, the procedures for dispute settlement under the above-mentioned Article were not specified in the agreement but, rather, developed over the years through State practice until formulated in a written Understanding in 1979.<sup>91</sup> During the initial years, the parties' tendency to distance themselves from any process of judicial character was very evident. Instead, disputes were discussed in the plenary assembly of the CONTRACTING PARTIES, where the participants

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<sup>85</sup> See generally *Australian Subsidy on Ammonium Sulphate*, *supra* note 83, and *Treatment by Germany of Imports of Sardines*, *supra* note 83.

<sup>86</sup> GATT, *supra* note 36, art. XXIII.

<sup>87</sup> *Id.*

<sup>88</sup> GATT, *supra* note 36, art. XXIII. GATT also provides for the right of consultation. *Id.* art. XXII.

<sup>89</sup> *Id.*

<sup>90</sup> *Id.*

<sup>91</sup> Understanding Regarding Notification, Consultation, Dispute Settlement and Surveillance, Nov. 28, 1979, GATT B.I.S.D., (26th Supp.) at 210, 216 (1980) [hereinafter Understanding Regarding Dispute Settlement].

were diplomats and where every decision had to be taken unanimously.<sup>92</sup> Naturally, diplomats sought solutions which were acceptable to all parties, including the party in breach of its obligations. Some of the disputes were also transferred to "working parties" which too were made up of representatives of a number of countries.<sup>93</sup> These representatives were not intended to be independent but could receive instructions from their governments with regard to the desired solution to the particular dispute.<sup>94</sup> In 1955, a change of approach took place. Disputes were placed before a panel of neutral experts, who would act according to their own understanding and not as representatives of their governments.<sup>95</sup> This change was a first step in the juridicization process of dispute settlement under GATT away from a system entirely based on negotiations within a multilateral diplomatic framework toward a process much more legal in nature and whose purpose is to objectively examine the facts and achieve a correct interpretation of the provisions of the agreement.

Since then, the use of panels has prevailed. The panels are used as bodies which fulfill the function of investigating the dispute placed pursuant to Article XXIII before the CONTRACTING PARTIES (which act through the GATT Council) and, afterwards, presenting their conclusions and recommendations to the Council. However, authority is retained by the Council, as provided in the above Article. Accordingly, the recommendations of the panel have no binding effect whatsoever unless adopted by the Council.<sup>96</sup> Despite the fact that, formally, the agreement allows decisions to be reached by majority vote on the basis of one vote per State,<sup>97</sup> in practice, all the work of the Council is based on the *de facto* rule that all decisions are made unanimously.<sup>98</sup> The application of this rule to dispute settlement pro-

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<sup>92</sup> HUDEC, *supra* note 4, at 29.

<sup>93</sup> *Id.* at 29-30.

<sup>94</sup> See JACKSON, *supra* note 3, at 95. See also Understanding Regarding Dispute Settlement, *supra* note 91, Annex, art. 6(i).

<sup>95</sup> See JACKSON, *supra* note 3, at 95. See also Understanding Regarding Dispute Settlement, *supra* note 91, art. 14. This article states, "Panel members would serve in their individual capacities and not as government representatives, nor as representatives of any organization. Governments would therefore not give them instructions nor seek to influence them as individuals with regard to matters before a panel. Panel members should be selected with a view to ensuring the independence of the members, a sufficiently diverse background and a wide spectrum of experience."

<sup>96</sup> See Understanding Regarding Dispute Settlement, *supra* note 91, art. 16.

<sup>97</sup> See GATT, *supra* note 36, art. XXV.

<sup>98</sup> See HUDEC, *supra* note 4, at 8. See also Pierre Pescatore et al., 1982 Ministerial Declaration on Dispute Settlement, in HANDBOOK OF WTO/GATT DISPUTE SETTLEMENT 21, 23 (Kluwer Law & Taxation Publishers, 1996).

cedures creates the problematic situation in which the defending party is able to "block" any such procedures directed against it. The power to block is, in practice, available at every stage of the proceedings, from the appointment of the panel, its composition, the formulation of its terms of reference to the decision whether or not to adopt the recommendations of the panel. Even if the panel's recommendations are adopted but the defendant refrains from obeying them, the latter's consent is required to permit the retaliatory measures which the GATT Council may authorize the injured State to take!

For an ordinary lawyer not familiar with the niceties of international diplomacy, the need to obtain the agreement of the "losing" party to adopt the decision against it, seems to deprive the entire proceedings of their significance and make them completely redundant. In order to resolve a dispute by agreement, one may argue, there is no need for an arbitration procedure. Indeed, why should a party agree to stop violating its obligations if, in any event, it is not possible to apply sanctions against it without its consent?

There is no doubt that the requirement of consensus significantly impaired the legal nature of the GATT agreement and "the rule of law" in the arena of international trade relations. However, it would be a mistake to think that the GATT enforcement procedures were worthless. On the contrary, this mechanism worked fairly well in practice, considering the circumstances for almost fifty years, and this is borne out by the fact that many States have utilized it. In the 1980s, there was a 300% growth in the number of legal proceedings within the GATT framework.<sup>99</sup> Almost every application for the appointment of a panel was ultimately honored (even if occasionally after lengthy delays), and most of the recommendations of the panels were adopted in the end (again, on occasion after long delays).<sup>100</sup> Once adopted, the recommendations were generally respected and implemented by the States involved. Except for one case in the 1950s,<sup>101</sup> it

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<sup>99</sup> See Robert E. Hudec, *Dispute Settlement*, in *COMPLETING THE URUGUAY ROUND: A RESULTS ORIENTED APPROACH TO THE URUGUAY ROUND TRADE NEGOTIATIONS* 180, 182 (Jeffrey J. Schott ed., 1990).

<sup>100</sup> *Id.* at 181-82.

<sup>101</sup> This was the case involving a dispute between Holland and the United States regarding U.S. restrictions on the import of milk products from Holland. Following a complaint by Holland which was found to be justified, Holland was empowered to take retaliatory measures against the United States. *Netherlands Measures of Suspension of Obligations to the United States*, Nov. 8, 1952, GATT B.I.S.D. (1st Supp.) at 32 (1953). Even though authorized to impose quotas on grain imports from the United States for seven consecutive years, the Netherlands never made use of their power because of the ineffectiveness of this measure against such a large country as the United States. See JACKSON, *supra* note 3, at 96.



never became necessary to take retaliatory steps against a State refusing to honor the recommendations of the Council.<sup>102</sup> However, the blocking power was frequently exploited by States which were the subjects of complaints at preliminary stages of the process. Often the blocking led only to delays. Sometimes, however, the defendant State succeeded in extracting a legal or procedural advantage by virtue of its blocking power.<sup>103</sup> Occasionally, an injured party was forced to compromise and accept only a partial implementation of the panel's recommendations.<sup>104</sup>

The explanation for the fact that the mechanism nevertheless worked in a reasonable fashion up to the 1980s lies in the mutual interest of all the GATT Parties in the efficient functioning of the agreement. The Fourth part of this article will discuss more extensively the considerations and interests operating in this area. At this stage, it is sufficient to point to the fact that a State which today finds itself losing in a legal proceeding before a GATT panel may tomorrow find itself winning another such proceeding. Just as the State expects that a decision in its favour is honored, it is clear that it must also honor a decision given against it. There is a significant difference between a situation where a State is involved in a trade dispute where no impartial ruling on the disputed question has been delivered (and when State officials often have a myriad of arguments to justify their action) and the situation where all the arguments have already been heard and rejected by a panel of independent arbitrators. No State is keen to be regarded as an "international offender" in the eyes of the international community. At this stage, refusal to abide by the decision of the arbitrators, a decision which enjoys support of other GATT parties who are willing to adopt it, is tantamount to undermining the entire regime of GATT in which all parties have a vested interest. Nevertheless, this important consideration is only one of the

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<sup>102</sup> In 1988-1989, the United States in fact blocked two requests to authorize retaliatory steps, one made by the European Community and the other by Canada, by refusing for a period of 3 years to abide by the GATT Council decision against one of the United States tax laws which were found to be contrary to the provisions of the agreement. See Hudec, *supra* note 99, at 184.

<sup>103</sup> Hudec, *supra* note 99, at 182.

<sup>104</sup> Thus, for example, in the dispute between Mexico and the United States in relation to the restrictions on the import of tuna, Mexico agreed not to demand the full adoption and enforcement of the decision made in its favor. Restrictions on Imports of Tuna, GATT B.I.S.D. (39th Supp.) at 155 (1991), *reprinted in* 30 I.L.M. 1594 (1991). The United States made only partial amendments to its domestic legislation which had been found to be in breach of the GATT rules. A number of infringing laws were not modified as shown by the later filing by the European Community of the second complaint made in this regard. For a review of these proceedings, see, e.g., Paul J. Yechout, *In the Wake of Tuna II: New Possibilities for GATT-Compliant Environmental Standards*, 5 MINN. J. GLOBAL TRADE 247 (1996).

considerations likely to guide the decision-makers. It may very well be counter-balanced by weighty internal political interests at odds with the decision and in favor of maintaining the protectionist measure. In such a case, a politician may be tempted to prefer his own short-term interests over the long-term interests of his State.

From the above, it is clear that the possibility of blocking legal proceedings impairs the effectiveness of the enforcement procedures of GATT, and, to use Professor Jackson's terminology, opens the door to "power oriented diplomacy" instead of "rule oriented diplomacy."<sup>105</sup>

## 2. *Dispute Settlement in GATT Following the Uruguay Round*

The juridicization process of the GATT enforcement procedures reached its present climax following the Uruguay Round of Multilateral Trade Negotiations (Uruguay Round). The dispute resolution agreement resulting from the Uruguay Round has been described as a triumph of the lawyers over diplomats.<sup>106</sup>

This agreement reached during the Uruguay Round surprised many, including many commentators, in view of the fact that, at the outset of the negotiations, most of the parties opposed the repeal of the consensus requirement and the vetoing power which in effect conferred on every State.<sup>107</sup> They were of the opinion that, in any event, the GATT rules would never be sufficiently strong to force rejectionist States to obey.<sup>108</sup> They believed that it would be preferable to retain the flexibility which the existing mechanism allowed the parties with regard to their obligations.<sup>109</sup> The more flexible mechanism made the parties more willing to accept far-reaching obligations with the knowledge that, in difficult cases, they would always have a certain way out.<sup>110</sup>

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<sup>105</sup> See JACKSON, *supra* note 3, at 85-88. Thus, for example, Prof. Hudec points to 17 cases of significant use of the blocking power in 57 legal determinations delivered by GATT panels between the years 1957-1989. See Hudec, *supra* note 99, at 183.

<sup>106</sup> See Michael K. Young, *Dispute Resolution in the Uruguay Round: Lawyers Triumph over Diplomats*, 29 INT'L LAW. 389, 406 (1995) (describing how the dispute resolution process under GATT after the Uruguay Round appears "very judicial and adjudicatory in character and application").

<sup>107</sup> Hudec, *supra* note 99, at 184.

<sup>108</sup> *Id.*

<sup>109</sup> *Id.*

<sup>110</sup> *Id.* at 185.

In the "Midterm Agreement" on dispute settlement, drafted in 1989 prior to the conclusion of the Uruguay Round,<sup>111</sup> the parties reiterated their commitment to the requirement of consensus,<sup>112</sup> while rejecting the proposal for "consensus minus two,"<sup>113</sup> which provided for consensus of all of the Members of GATT less the two disputing parties. Nevertheless, the Midterm Agreement represents a further milestone in the juridicization process, as a number of other improvements were incorporated into the Midterm Agreement which have the effect of strengthening the enforcement process of dispute settlement. For example, one improvement contained in the Midterm Agreement is the provision for a maximum time-table for the different stages of the dispute resolution process which is designed to prevent protracted delays during arbitration of disputes.<sup>114</sup> Similarly, a number of provisions were made with the aim of eliminating the power to block the dispute resolution process in the early stages of a dispute in order to secure the completion of the arbitration process.<sup>115</sup> As will be seen, these provisions were ultimately incorporated in the final agreement of the Uruguay Round (Final Act),<sup>116</sup> which introduced the most significant modification to the existing dispute resolution process.

Upon the establishment of the WTO in 1994 by the Final Act,<sup>117</sup> the GATT dispute settlement mechanism received appropriate institutional support in the form of a new organ, the Dispute Settlement

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<sup>111</sup> Conciliation, Improvements to the GATT Dispute Settlement Rules and Procedures, GATT B.I.S.D. (36th Supp.) at 61 (1990) [hereinafter Midterm Agreement].

<sup>112</sup> *Id.* art. G.3.

<sup>113</sup> Hudec, *supra* note 99, at 186.

<sup>114</sup> The Midterm Agreement provided that the initial bilateral consultation process must end within 60 days. Midterm Agreement, *supra* note 111, art. C.2. If the dispute is not settled within this period of time, the complainant State may request the appointment of a panel. *Id.* It is further provided that this request will be heard and decided at the most at the second meeting of the GATT Council, following the presentation of the request. *Id.* art. F(a). However, there is no express provision for the right of the complainant to a panel in relation to his complaint.

<sup>115</sup> Standard terms of reference for the arbitrators were provided. Midterm Agreement, *supra* note 111, art. F(b). In practice, these were built on the complaint presented by the complainant, save where the parties agreed on a different formulation. *Id.* Similarly, power was conferred upon the Director-General of GATT to appoint the members of the panel in the absence of agreement between the parties. *Id.* art. F(c)(5).

<sup>116</sup> Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations, Apr. 15, 1994, LEGAL INSTRUMENTS - RESULTS OF THE URUGUAY ROUND vol. 1 (1994), 33 I.L.M. 1125 (1994) [hereinafter Final Act].

<sup>117</sup> *Id.* at 1143 para. 1. In the Final Act, the participants of the Uruguay Round agreed to the Agreement Establishing the World Trade Organization. See Agreement Establishing the World Trade Organization, reprinted in Final Act, *supra* note 116, at 1144 [hereinafter WTO Agreement]. The WTO Agreement establishes the WTO. WTO Agreement, *supra* note 42, art. 1.

Body (DSB).<sup>118</sup> As evidenced by its name, the DSB is concerned solely with the settlement of trade disputes in connection with the GATT accord.<sup>119</sup> The DSB is composed of representatives from all the WTO members.<sup>120</sup> In dealing with disputes, the DSB acts in accordance with the rules set out in the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU), which is annexed to the WTO Agreement.<sup>121</sup> These rules are primarily based on the panel system, as developed over the years and as improved in the 1979 and 1989 agreements.<sup>122</sup> However, in the DSU, a number of very important changes were made to the dispute resolution process which may be justly characterized as a revolution in the GATT approach to dispute settlement. As discussed below, the important changes illustrating the juridicization process in the dispute resolution process include: (1) the affirmation of the exclusive character and legal primacy of the DSU dispute resolution system; (2) the establishment of a strict time table for each stage in the dispute resolution process; (3) the revocation of the power to block procedures; (4) the duty to terminate the infringement of GATT; (5) the duty to adopt the panel's recommendations; (6) the establishment of an appellate body; (7) surveillance on the implementation of recommendations and rulings; (8) restrictions on the non-legal grounds of complaint; and (9) possibility of cross-retaliation.

a. The Affirmation of the Exclusive Character and Legal Primacy of DSU Dispute Resolution

Under the heading "Strengthening of the Multilateral System," Article 23 of the DSU sets out several obligations whose aim is to ensure that in case disagreements, WTO Members will not have recourse to any alternative dispute settlement methods outside the

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<sup>118</sup> The WTO Agreement provides that the WTO will administer the Understanding on Rules and Procedures Governing the Settlement of Disputes. WTO Agreement, *supra* note 109, art. III:3. The Understanding on Rules and Procedures Governing the Settlement of Disputes is annexed to the Final Act. See Final Act, *supra* note 116, Annex 2, 33 I.L.M. at 1226 [hereinafter DSU]. The DSU establishes the Dispute Settlement Body (DSB). *Id.* art. 2.1.

<sup>119</sup> See DSU, *supra* note 118, art. 2.1.

<sup>120</sup> The WTO Agreement creates a General Council which is composed of all Members. WTO Agreement, *supra* note 42, art. IV:2. Under the WTO Agreement, the General Council will convene to discharge the responsibilities of the DSB. *Id.* art. IV:3. Thus, the DSB is composed of all Members.

<sup>121</sup> See Final Act, *supra* note 116, Annex 2, 33 I.L.M. at 1226.

<sup>122</sup> See generally Midterm Agreement, *supra* note 111, art. F (describing panel and working party procedures).

WTO.<sup>123</sup> It also clearly precludes any unilateral action by one Member against another, justified for example by the claim that obligations have been violated. Members are required to first obtain a determination to that effect through the DSU process,<sup>124</sup> and may only suspend concessions or other obligations following an authorization by the DSB.<sup>125</sup> Unilateral unauthorized trade sanctions, such as those employed in the past under the U.S. Section 301, would therefore be inconsistent with GATT.<sup>126</sup>

b. The Establishment of a Strict Time Table for Each Stage in the Process

Some of the provisions with regard to establishing strict time tables for the dispute resolution process are taken from the Midterm Agreement of 1989.<sup>127</sup> Maximum time periods are set for consultation,<sup>128</sup> the establishment and composition of panels,<sup>129</sup> panel hearings and the delivery of panel decisions,<sup>130</sup> the process of adopting the recommendations of the panel,<sup>131</sup> and, finally, for implementation of the recommendations.<sup>132</sup>

c. Revocation of the Power to Block Procedures

Following the example of the Midterm Agreement, the DSU adopts the "default mechanism" in order to prevent the possibility of an interested party blocking the process. Thus, a panel will be established if a complainant party so requests, unless the DSB decides by consensus not to create a panel.<sup>133</sup> The terms of reference of the

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<sup>123</sup> DSU, *supra* note 118, Article 23:1. This provision requires Members who seek redress of a violation of WTO obligations or other nullification or impairment of benefits to "have recourse to, and abide by" the rules and procedures of the DSU.

<sup>124</sup> *Id.* art. 23:2(a).

<sup>125</sup> *Id.* art. 23:2(c).

<sup>126</sup> On this debated issue, *see, e.g.*, SERVICES OF THE EUROPEAN COMMISSION, REPORT ON THE UNITED STATES BARRIERS TO TRADE AND INVESTMENT 7 (1994) (arguing that U.S. efforts to renew "Super 301" are inconsistent with WTO provisions); JOHN JACKSON, DISPUTE SETTLEMENT PROCEDURES IN OECD, THE NEW WORLD TRADING SYSTEM: Readings 117, 120 (1994); and Jared R. Silverman, *Multilateral Resolution over Unilateral Retaliation: Adjudicating the Use of Section 301 Before the WTO* 17 U. PA. J. INT'L ECON. L. 233 (1996).

<sup>127</sup> *See generally* Midterm Agreement, *supra* note 111.

<sup>128</sup> *See* DSU, *supra* note 118, art. 4.3, 4.7, 4.8, 4.11.

<sup>129</sup> *Id.* arts. 6.1, 8.5, 8.7.

<sup>130</sup> *Id.* arts. 12.5, 12.8, 12.12, 15.2, 15.3.

<sup>131</sup> *Id.* arts. 16.1, 16.2, 16.4.

<sup>132</sup> *Id.* art. 21.3-6.

<sup>133</sup> *Id.* art. 6.1.

panel are standard unless the parties agree to another formulation.<sup>134</sup> The standard terms of reference delineate the boundaries of the panel's jurisdiction over the dispute and the legal issues raised in the complainant's request for the establishment of a panel.<sup>135</sup> Thus, the complainant is in effect given the right to define the substantive jurisdiction of the panel, and defendants can no longer block various legal issues or claims from being heard by the panel. Furthermore, the panel is expressly required to address the relevant provisions in any agreement cited by the parties to the dispute,<sup>136</sup> another indication of the legal nature of the proceedings.

Likewise, various provisions are introduced in the DSU regarding the composition of the panels. The DSU provides that panel members will be selected from a list of well-qualified individuals, compiled by the DSB secretariat and including both government officials and private persons.<sup>137</sup> These panelists will be independent and will possess the widest possible qualifications and experience.<sup>138</sup> The panelists will also be citizens of countries other than those of the litigants or of the third parties involved in the dispute.<sup>139</sup> If the parties disagree as to the composition of the panel, the Director General of the WTO, "in consultation with the Chairman of the relevant Council of Committee," shall appoint the members of the panel.<sup>140</sup>

#### d. The Duty to Terminate the Infringement of GATT

For the first time, the GATT dispute resolution process provides binding instructions on the preferred course of action in cases of infringements. Panels which have found a certain measure to be inconsistent with a covered agreement must recommend that the infringing State "bring the measure into conformity with that agreement."<sup>141</sup> In

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<sup>134</sup> *Id.* art. 7.1. Article 7.1 provides the following default terms of reference, "To examine, in the light of the relevant provisions in (name of covered agreement(s) cited by the parties to the dispute), the matter referred to the DSB by (name of party) in document. . .and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in that/those agreement(s)." *Id.*

<sup>135</sup> *Id.* art. 7.1

<sup>136</sup> *Id.* art. 7.2.

<sup>137</sup> *Id.* arts. 8.1, 8.4.

<sup>138</sup> *Id.* art. 8.2.

<sup>139</sup> *Id.* arts. 8.2, 8.3.

<sup>140</sup> *Id.* art. 8.7.

<sup>141</sup> *Id.* art. 19.1. In addition, where the recommendations or rulings of the panel are not implemented within a reasonable period of time, the DSU provides for temporary compensation (generally meaning an alternative benefit and not a money payment) and suspension of concessions or other obligations. *Id.* art. 22.1. However, compensation and suspension of concessions should not be preferred to bringing the infringing measure into conformity with GATT.

the past, no such instruction existed. Past panels that found measures inconsistent with GATT refrained from demanding the termination of the breach, but were satisfied with action which had the effect of compensating the injured parties or preventing the injury to them.<sup>142</sup> Therefore, the new provision entrenches the binding effect of GATT law.

e. The Duty to Adopt the Panel's Recommendations

In contrast to the situation prevailing in GATT for close to fifty years, in which the adoption of the recommendations had to be by consensus, today the position is completely different. Within sixty days from the publication of the panel report, DSB is obliged to adopt the report unless there is a consensus not to adopt them.<sup>143</sup> Not only have WTO Members now agreed to waive the requirement of unanimous adoption, something they refused to do in 1989, but, in practice, they have also completely waived the "political filter" in the form of the GATT Council with regard to the legal determinations of the panels. The current dispute resolution procedures do not provide for a majority decision or a "consensus minus two," which, under an Uruguay Round proposal, would require a majority excluding the two States involved in the dispute. Instead, the current procedures have created a process where the recommendations of the panels are automatically adopted, except where the winning State itself agrees that they should not be adopted.

f. The Establishment of an Appellate Body

As a replacement for the political review over the panels' recommendations, the States agreed to establish a legal system of appeals (the Appellate Body).<sup>144</sup> This instance, contrary to the panels previously established ad hoc for each specific dispute, is a permanent body whose function is to hear appeals against the decisions of the panels on legal questions only.<sup>145</sup> Therefore, here we have a formal and official recognition of the legal facet of the GATT regime and the need to

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<sup>142</sup> See, for example, the decision in the dispute between Australia and France in relation to the subsidy on wheat. French Assistance to Export of Wheat and Wheat Flour, Nov. 22, 1958, GATT B.I.S.D. (7th Supp.) at 22 (1959).

<sup>143</sup> DSU, *supra* note 118, art. 16.4. In addition, the DSB is not obliged to adopt the panel's decision if one of the parties to the dispute has given notice of its intention to appeal the panel's decision.

<sup>144</sup> See generally, DSU, *supra* note 118, art. 17.

<sup>145</sup> *Id.* art. 17:6. "An appeal shall be limited to issues of law covered in the panel report and legal interpretations developed by the panel." *Id.*

give it a uniform and binding legal interpretation. To hear appeals, the DSB will establish a standing Appellate Body.<sup>146</sup> The Appellate Body will be comprised of seven permanent members "of recognized authority, with demonstrated expertise in law, international trade and the subject matter of the covered agreements generally."<sup>147</sup> The decision of the Body shall also be adopted by the DSB, unless there is a consensus not to adopt it.<sup>148</sup>

The establishment of the Appellate Body has enormous potential to entrench the juridicization process within the GATT framework. Even though formally, a decision of the Appellate Body is only binding upon the parties to the dispute in that particular case, in practice GATT panels customarily do rely on past precedents, and the Appellate Body's rulings and interpretations are very likely to enjoy *de facto* status of *stare decisis*. The body will therefore be able to ensure a uniform and consistent development of GATT jurisprudence, in contrast to the sporadic and occasionally inconsistent panel decisions given to date. This jurisprudence will be able to guide the legal advisors of the WTO Members, as well as future panels whose decisions will be subject to review by the Appellate Body. It is difficult not to draw an analogy to the EC Court of Justice. If the GATT Appellate Body succeeds in achieving even a small part of what has been achieved by the EC Court of Justice, it would be of great value. It is, of course, quite unlikely that the Appellate Body of the WTO will be able to follow a policy of teleological interpretation and judicial activism such as that adopted by the EC Court of Justice. Not only are political constraints at play here, but there also exists an express provision prohibiting the panels and Appellate Body from adding or detracting from "the rights or obligations set out in the agreements."<sup>149</sup> Nevertheless, the Appellate Body will be able to supply an agreed upon and clear interpretation of the existing provisions, thereby resolving some of the intense conflicts in international trade law.

g. Surveillance on the Implementation of Recommendations and Rulings

The DSB has a duty to follow-up the implementation of the panels' recommendations and receive reports from the State required

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<sup>146</sup> *Id.* art. 17.1.

<sup>147</sup> *Id.* arts. 17:1, 17:3.

<sup>148</sup> *Id.* art. 17:14.

<sup>149</sup> *Id.* art. 19:2. Of course, the institutional difference and the differences between the integrative and political aims of the European Court of Justice, and those of the Appellate Body of the WTO, will dictate greater conservatism in the latter body.



to act thereunder.<sup>150</sup> The period of time allowed for implementing the recommendations is determined by the DSB or by agreement of the parties to the dispute.<sup>151</sup> It is also possible to proceed to binding arbitration in order to solve a disagreement on this point and to determine the reasonable period of implementation.<sup>152</sup>

h. Restrictions on the Non-Legal Grounds of Complaint

The non-legal grounds of complaint in GATT, otherwise called the Non-Violation Nullification or Impairment of Concessions,<sup>153</sup> have not been repealed. However, various restrictions have been imposed on them in order to narrow their scope and application. The DSU provides, "where a measure has been found to nullify or impair benefits under, or impede the attainment of objectives, of the relevant covered agreement without violation thereof, the panel, or Appellate Body, must recommend that the Member concerned make a *mutually satisfactory adjustment*,"<sup>154</sup> but there is no obligation to withdraw the measure.

i. Possibility of Cross Retaliation

It should be recalled that even if the panel's recommendations are adopted and become binding, there is of course no international "execution office" to enforce the panel's recommendations. Armed forces are not likely to be sent to enforce the injuring State's obligations under a trade agreement. Accordingly, the most extreme enforcement measure available takes the form of retaliatory action by the injured State against the injuring State with the authorization of the DSB.<sup>155</sup> The new agreement enables the injured State, provided that all diplomatic efforts have failed and that retaliatory measures in that sector and under the agreement in question are not practical, to take retaliatory measures in other sectors and to suspend obligations under other covered agreements.<sup>156</sup> For example, if a developing country is injured in the export of its merchandise to a developed country such as the United States, the developing country may in certain cases request permission to suspend its obligations to the United

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<sup>150</sup> See generally, *id.* art. 21.

<sup>151</sup> *Id.* art. 21.3(a)-(b).

<sup>152</sup> *Id.* art. 21.3(c).

<sup>153</sup> See *supra* note 83 and accompanying text.

<sup>154</sup> DSU, *supra* note 118, art. 26.1(b) (emphasis added).

<sup>155</sup> See generally *id.* art. 22.

<sup>156</sup> *Id.* "Covered Agreements" includes only the agreements that fall under the binding umbrella of the GATT 1994 and that are listed in Appendix 1 of the DSU. *Id.* art. 1.1.

States under the covered agreements relating to intellectual property or trade in services, a step which may prove to be more effective than imposing restrictions on U.S. goods. This right to suspend obligations under other covered agreements, known as the right to "cross retaliation," greatly strengthens retaliation as a sanction. Accomplished during the Uruguay Round, "cross retaliation" is the result of the integration of all the GATT agreements and their transformation into one binding complex.<sup>157</sup> Therefore, the enforcement measures available to the WTO are much more efficient than those available to other branches of public international law, and it suffices to recall the famous *Corfu Channel* case<sup>158</sup> in which there was no practical way of forcing Albania to pay the compensation awarded to the United Kingdom.

### 3. *Evaluation of the New Mechanism*

It is important to emphasize that this new mechanism still has not been tested in the short period of time since it came into force. A number of complaints have already been made against the dispute resolution mechanism. It will be very interesting to examine the functioning of the new mechanism, in particular, the political willingness of governments to honor the new dispute resolution mechanism and accept its determinations, especially when they are not favorable from an internal-political point of view.

One danger which recently threatened the mechanism, but which has since passed, is the intense dispute between the United States and Japan regarding the automobile trade.<sup>159</sup> The United States threatened to take unilateral retaliatory action against Japan in open violation of all the WTO principles, which require the transfer of disputes to an objective mechanism. Japan had already filed a complaint to the WTO regarding the blatant use by the United States of Section 301 of the United States Omnibus Trade and Competitiveness Act of 1988.<sup>160</sup> Had the issue been brought before a Panel, there is hardly a

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<sup>157</sup> See *supra* note 50 and accompanying text.

<sup>158</sup> See the decision of the International Court of Justice in the dispute between England and Albania over liability for explosions in the Corfu Channel, 1949 I.C.J. 4 (Apr. 9, 1949). By ten votes to six, the court reserved for consideration "the assessment of the amount of compensation." *Id.* at 36.

<sup>159</sup> William Drozdiak, *U.S., Japan Reach Trade Deal, Averting Sanctions*, WASH. POST, June 29, 1995, at A1; see also David E. Sanger, *U.S. Settles Trade Dispute, Averting Billions in Tariffs on Japanese Luxury Autos*, N.Y. TIMES, June 29, 1995, at A1 (detailing the events relating to the U.S.-Japanese settlement).

<sup>160</sup> See Omnibus Trade and Competitiveness Act of 1988 § 301, 19 U.S.C.A. § 2411 (1980 and Supp. 1996). The procedures under Section 301 of the U.S. Omnibus Trade and Competitiveness

doubt that a decision would have been delivered rejecting the unilateral use by the United States of retaliatory measures prior to applying for a dispute settlement procedure and without the agreement of the DSB. However, at the last minute, the parties reached a compromise and the conflict was avoided. The mere existence of the DSB, the fear of a panel decision unfavorable to the United States, and the possible collapse of the trade regime in the event that the United States ignored such an unfavorable decision were undoubtedly the factors that contributed to the United States' acceptance of the compromise. This incident is instructive in the sense that, in the arena of future international trade relations, there will still be room for threats as well as for international diplomacy. However, future international diplomacy will always be conducted in the shadow of the international law and enforcement mechanisms developed in recent years.

### III. JURIDICIZATION ON THE BILATERAL LEVEL: TRADE RELATIONS OF THE STATE OF ISRAEL

The evolutionary process which has transformed the multilateral framework of GATT may also be identified in regional and bilateral frameworks. It is of course impossible, in this setting, to examine the history of all such frameworks in order to demonstrate the juridicization process at work. It is sufficient to point to the proliferation of regional trade agreements in all regions of the world over the past decades, to the broadening of their scope and to the strengthening of their legal mechanisms.<sup>161</sup> In addition to the constantly evolving European Community, regional integration arrangements and initiatives such as NAFTA, ASEAN, MERCOSUR and APEC are some of the more prominent examples of this trend. Here, I shall confine myself to my own region and examine the history of Israel's bilateral trade agreements in order to prove the universal nature of the juridicization process.<sup>162</sup>

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Act of 1988 include a number of grounds and ways of acting with respect to which the government has a duty to act to open foreign markets by means of unilateral retaliatory measures, or threat of such measures, against a State by reason of its trading policy. See 19 U.S.C.A. §§ 2411-16. See also JACKSON, *supra* note 3, at 103-07 (discussing the use made of these legal provisions); JAGDISH BHAGWATI, *THE WORLD TRADING SYSTEM AT RISK* 48-57, 126-40 (1991).

<sup>161</sup> See, e.g., Andrew H. Hallet & Carlos A. Primo Braga, *The New Regionalism and the Threat of Protectionism*, Policy Research Working Paper 1349, The World Bank, 1994; John H. Jackson, *Regional Trade Blocs and GATT*, 16 *2 THE WORLD ECONOMY* 121-31 (1993).

<sup>162</sup> For a general overview of Israel's economy and foreign trade policy, see GATT SECRETARIAT, *GATT, TRADE POLICY REVIEW: ISRAEL* 1-2 (1995).

## A. Israel's Trade Relations with the EC up to 1995

Since its establishment in 1958, the EC has been the most important trading partner of the State of Israel. The more the EC expanded, the greater became its importance for Israel, particularly as a source for imports but also as a destination for Israel's exports. Thus, in 1994, 51% of the total goods imported to Israel originated in the EC, whereas 28.1% of total exports were directed there.<sup>163</sup> At the same time, the North-American market has increased in importance as a destination for Israeli exports. In 1994, it obtained a 31.7% share of total Israeli exports.<sup>164</sup>

### 1. *The Trade Agreement of 1964*

The first trade agreement between Israel and the EC was signed in 1964.<sup>165</sup> This agreement was very limited in scope. It applied only to a number of industrial goods and agricultural produce and did not even require the elimination of tariffs, but only partial reduction of custom duties and partial or total elimination of certain quantitative restrictions. The agreement did not contain any dispute settlement or enforcement mechanisms.<sup>166</sup> Further, the benefits given to the State of Israel by the agreement were later given to all GATT signatories, thereby in effect eroding its impact. In consequence, negotiations commenced for the signing of a new agreement.

### 2. *Trade Agreement of 1970*

Discussions in this regard commenced in June 1967. However, for political reasons, France imposed a veto on the renewal of contacts. Only in 1970, after the opposition was withdrawn, was a new preference agreement signed for a period of five years.<sup>167</sup> The scope of the new agreement was broad compared to the earlier agreement.

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<sup>163</sup> STATE OF ISRAEL, MINISTRY OF INDUSTRY & TRADE, *THE ISRAELI ECONOMY AT A GLANCE* 2-3 (1995).

<sup>164</sup> *Id.*

<sup>165</sup> Council Decision No. 64 *Treaties of the State of Israel* 15, p. 683 (Hebrew); Yaacov Cohen, *Implications of a Free Trade Area Between the EEC and Israel*, 10 J. WORLD TRADE L. 252 (1976).

<sup>166</sup> In fact a joint committee was set up comprising representatives of both sides for the purpose of reviewing the performance of the agreement, but it was empowered only to "propose to the competent bodies the measures which appeared to it to be appropriate" for the improvement of trade exchange. 1965 Agreement, Article 6. It did not serve as a dispute settlement body, and there is no reference in the agreement to the issues of dispute settlement or enforcement measures.

<sup>167</sup> EEC-Israel Trade Agreement of 1970, Council Decision No. 1526/70, 1970 J.O. (183) 1 [hereinafter 1970 Agreement].

Still, only about two-thirds of Israeli industrial exports and only a small part of its agricultural produce were covered by the 1970 agreement. The agreement did not lead to elimination of tariffs but only to a partial reduction thereof.<sup>168</sup> The agreement was not based on reciprocal concessions but was in the nature of a preference agreement between a developed country and a developing country, in which the latter was not required to give full consideration.<sup>169</sup> The agreement was very primitive in relation to any matter outside the specific tariff obligations, and, apart from the reference to the GATT agreements with regard to dumping practices and the grant of subsidies,<sup>170</sup> there were also no provisions whatsoever relating to non-tariff barriers. Like the 1964 agreement, the 1970 agreement failed to introduce any mechanism for dispute settlement or enforcement.<sup>171</sup>

### 3. *Agreement for the Establishment of a Free Trade Area, 1975 — First Generation FTAs*

A few years later, following the expansion of the EC (the accession of England, Ireland and Denmark) and the significant growth in trade between the parties, it was recognized that there was a need to create a general and comprehensive framework for the development of the economic relations between the parties.<sup>172</sup> This initiative was part of the EC's "Global Program for the Mediterranean Countries." This program aimed to establish bilateral agreements between the EC and all the countries of the Mediterranean which would take the form of agreements to establish free trade areas (FTAs) for industrial goods. Such an agreement was signed between Israel and the EC in 1975.<sup>173</sup>

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<sup>168</sup> See Cohen, *supra* note 165, at 252.

<sup>169</sup> See GATT, *supra* note 36, art. XXXVI (added in 1966), regarding the relations between developing and developed countries, which provides, *inter alia*, that in these relations the developed countries shall not expect reciprocity in terms of their undertakings towards the developing countries.

<sup>170</sup> 1970 Agreement, *supra* note 167, art. IX.

<sup>171</sup> See generally *supra* note 165.

<sup>172</sup> Cohen, *supra* note 165, at 253.

<sup>173</sup> Agreement Between the European Economic Community and the State of Israel, May 20, 1975, Isr.-E.E.C., 18 O.J. EUR. COMM. (No. L. 136) (1975) [hereinafter 1975 Agreement]. For an extensive discussion of the 1975 Agreement, see TALIA EINHORN, *THE ROLE OF THE FREE TRADE AGREEMENT BETWEEN ISRAEL AND THE EEC: THE LEGAL FRAMEWORK FOR TRADING WITH ISRAEL BETWEEN THEORY AND PRACTICE* (Baden-Baden: Nomos Recht, 1994); J.H.H. Weiler, *Israel and the EEC: A New Legal Model for Trade and Cooperation*, 3 JEWISH L. ANN. 196; S.H. Langer, *The Israel-EEC Free Trade Agreement: An Analysis of the Agreement and its Effect on Investments*, 9 SYR. J. INT'L L. & COM. 63 (1982).

The 1975 agreement was Israel's first free trade agreement with any country. It set the stage for numerous other agreements, which will be discussed later. This agreement created the first general substantive framework for regulating the two parties' trade relations on the basis of a gradual elimination of tariff and non-tariff trade barriers. It was this agreement, and not the fifteen-year membership in GATT, which gave the first push towards real liberalization of Israel's foreign trade policy. Nevertheless, the agreement must be classified as a "first generation" FTA agreement, in terms of its "juridical" nature, as defined above. This is true both on the substantive level, principally in relation to the manner of regulation of non-tariff barriers, and on the institutional level, i.e., dispute settlement and enforcement mechanisms. This claim shall be proved hereunder by pointing to some of the limitations and flaws of the agreement.

a. Limitations on the Substantive Level

The primary function of the FTA agreement of 1975 was undoubtedly the gradual elimination of tariffs on trade in goods. Here, special consideration was given to the State of Israel in light of its economic level of development at that time, and, therefore, the reduction of Israeli tariffs was performed over a period of fourteen years until their final elimination in 1989.<sup>174</sup> EC tariffs on goods from Israel, in contrast, were eliminated within one and one-half years of the signing of the agreement.<sup>175</sup> However, the elimination of tariffs applied only to industrial goods; in the area of agriculture, tariffs were not eliminated, and other trade barriers, such as quotas and subsidies, were also maintained.<sup>176</sup>

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<sup>174</sup> Originally, the reduction was due to be completed by 1985 under Protocol 2 of the 1975 Agreement, but Israel utilized its right under Article 22 of the agreement and requested two postponements of 2 years each. See Council Regulation No. 1008/81, 1981 J.O. (102) 1 (presenting Second Additional Protocol to E.C.-Israel FTA that extended time-table from January 1, 1985, to January 1, 1987); and Council Regulation No. 3565/84, 1984, J.O. (332) 1 (presenting Third Additional Protocol that extended time-table to January 1, 1989). Accordingly, Israeli tariffs on EC industrial goods were in fact eliminated only on January 1, 1989.

<sup>175</sup> Reduction of EC tariffs are regulated in Protocol No. 1 of the agreement, under which a 100% reduction was carried out by January 7, 1977 on industrial products, other than those special exceptions enumerated in Protocol 1 of the 1975 Agreement.

<sup>176</sup> See 1975 Agreement, *supra* note 173, Protocol 1. This protocol provides for only limited reduction of tariffs in relation to processed agricultural products. Similarly, Article 5 of the 1975 Agreement provides that the prohibitions on the imposition of new tariffs and quotas provided in Articles 3 and 4 will not apply to agricultural products listed in Annex 2 of the Treaty of Rome. Accordingly, specific arrangements were made in relation to agricultural products, and Article 7 of the 1975 Agreement provides that these arrangements will be subject to amendment in the event of a change in the agricultural policy of one of the parties.

In relation to the regulation of non-tariff barriers, the agreement is somewhat lacking. There is a general prohibition in Article 3 on the imposition of any new customs duties or "charges having equivalent effect," as well as any quantitative restrictions or "measures having equivalent effect."<sup>177</sup> Similar provisions are found in the Treaty of Rome which established the EEC,<sup>178</sup> in Articles 12 (charges with equivalent effect) and 30 (quantitative restrictions and measures with equivalent effect), and there they have been given a broad interpretation by the European Court of Justice.<sup>179</sup> However, the FTA agreement does not feature an international judicial tribunal equivalent to the European Court, and it is not clear whether such interpretation would also be acceptable here. In any event, Article 3 only applies to restrictions on imports, whereas restrictions on exports are subject to Article 4. This latter provision is narrower and does not prohibit quantitative restrictions or measures of equivalent effect. On the basis of this distinction, the United Kingdom, for example, placed an embargo on the export of oil to Israel, a prohibition which could not be attacked under the terms of the agreement.<sup>180</sup>

The agreement does contain provisions prohibiting the operation of discriminatory measures of an internal fiscal nature,<sup>181</sup> freeing from restrictions payments for goods traded under the agreement,<sup>182</sup> provisions relating to the adoption of anti-dumping measures,<sup>183</sup> as well as a prohibition against measures which distort competition, such as cartels, exploitation of a dominant position, and public aid.<sup>184</sup> This latter

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<sup>177</sup> 1975 Agreement, *supra* note 173, art. III.

<sup>178</sup> Treaty Establishing the European Economic Community, Mar. 25, 1957, 298 U.N.T.S. 11 [hereinafter Treaty of Rome].

<sup>179</sup> For a comprehensive overview of the Court's case law on these provisions, see W. RAWLINSON & M.P. CORNWELL-KELLY, *EUROPEAN COMMUNITY LAW* 34-39 (1990).

<sup>180</sup> See the affair considered by the European Court of Justice in Case 174/84 Bulk Oil (Zug) A.G. v. Sun International Ltd., 2 C.M.L.R. 732 (1986).

<sup>181</sup> 1975 Agreement, *supra* note 173, art. IX.

<sup>182</sup> 1975 Agreement, *supra* note 173, art. X. Reference is to foreign currency control regulations, which may not restrict the removal of currency from the State or the purchase of currency from Israel in connection with the trade in goods to which the agreement applies.

<sup>183</sup> 1975 Agreement, *supra* note 173, art. XIV. The article provides that any anti-dumping measures adopted by any of the parties is to be subject to the restrictive provisions of the Anti-Dumping Code of GATT, known as "The Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade" (then, the Kennedy Round Anti-Dumping Code). This was an innovation, as the State of Israel was not a party to the GATT Anti-Dumping Code until 1995, upon the coming into force of the Uruguay Round agreement. The above Article, therefore, required Israel to act in accordance with the Anti-Dumping Code in its relations with the EC only, even though Israel had not acceded to this code.

<sup>184</sup> 1975 Agreement, *supra* note 173, art. XII. See also ERAN LEV, *EUROPEAN COMMUNITY LAW: RELEVANT ASPECTS FOR THE ISRAELI LAWYER AND BUSINESSMAN* 195-97 (Hebrew).

prohibition is also very similar to the provisions set out in the Treaty of Rome in Articles 85, 86 and 92 respectively, provisions which have been interpreted broadly and implemented vigorously by the EC institutions.<sup>185</sup> This, however, does not mean that the same could be done with the competition rules of the FTA. The differences in the institutional setting (there is no equivalent in the FTA to the powerful institutions of the EC—the Commission and the Court) and in the objectives of the two regimes (a common market as opposed to a free trade area) lead to the conclusion that the scope of the rules differ.<sup>186</sup> The agreement also does not contain any reference to the issue of government procurement and the trade barrier arising out of Buy National policies practiced by government agencies in their purchases. There is also no reference to import licence requirements (which at the time were common in Israel),<sup>187</sup> trade in services or intellectual property, or to trade related investment measures (such as TRIMS).<sup>188</sup> All of these provisions may be found in “second generation” and later FTA agreements, as will be seen below.

Finally, it should be pointed out that the Protocol on Rules of Origin that apply to trade under the agreement contains a number of hidden traps, which in effect are disguised trade barriers.<sup>189</sup> Reference is made to Protocol No. 3, as amended in 1976.<sup>190</sup> Protocol No. 3 determines which products shall be deemed to be products originating in Israel or in the EC, respectively and, thus, will be entitled to duty-free treatment and to the other benefits of the agreement. The purpose of the rules is to prevent the situation where a third State will take a free-ride on the FTA by exporting its products to the EC through the State of Israel, or *vice-versa*, in order to avoid custom

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<sup>185</sup> See generally RICHARD WHISH, *COMPETITION LAW* (2d ed. 1989); BELLAMY & CHILD, *COMMON MARKET LAW OF COMPETITION* (4th ed. 1993).

<sup>186</sup> Lev also takes this view. LEV, *supra* note 184, at 196, as does BELLAMY & CHILD, *supra* note 185, at 135. Upon signing the FTA, the EC declared that when applying Article 12 of the 1975 Agreement it would apply the laws relating to Articles 85, 86, 90 and 92 of the Treaty of Rome, but this was a unilateral declaration to which the State of Israel was not a party. See 1975 Agreement, *supra* note 173, at 243 (declaration of the EC attached to the agreement).

<sup>187</sup> This licensing was carried out under the Import and Export Ordinance (New Version) - 1979, Laws of the State of Israel (New Version) 32 (1979) p. 625, and the various orders promulgated thereunder. See EINHORN, *supra* note 173, at 52-57.

<sup>188</sup> WTO Agreement, *supra* note 42, Annex 1A:14.

<sup>189</sup> On Rules of Origin in international trade generally and on the use of them to create concealed trade barriers, see RULES OF ORIGIN IN INTERNATIONAL TRADE: A COMPARATIVE STUDY (Vermulst et al. eds., 1994).

<sup>190</sup> Decision No. 2/76 of the Joint Committee amending Protocol No. 3 of the agreement between the European Economic Community and the State of Israel regarding Rules of Origin, Treaties of the State of Israel 28, 57; O.J. EUR. COMM. (No. L. 190) (1977).



duties; this is indeed a legitimate goal. It should be recalled that international trade is based on the principle of reciprocity, and States which have not given "consideration" cannot enjoy the benefits conferred within the framework of a reciprocal agreement between other States. Accordingly, to be eligible for the benefits of the FTA, a product must either wholly originate within the territory of one of the parties or be a product manufactured from other components which do not fall into the above category but in the making of which sufficient work or processing has taken place.

In this regard, Protocol No. 3 provides for the change-of-tariff-classification-test for determining the origin of a product in that only a product exported to the EC under a tariff classification different from the classification of all its components will be recognized as an Israeli product.<sup>191</sup> However, this rule is subject to numerous exceptions where other conditions may apply.<sup>192</sup> Many of these exceptions impose very strict requirements so that many products exported from Israel are unable to enjoy the duty-free treatment under the agreement. Thus, for example, in the area of textiles, there is a requirement for two tariff classification changes, and not just one. For example, ties and other clothing designed and sewn in Israel from cloth made outside Israel are not deemed to be products originating in Israel unless the cloth too is made there.<sup>193</sup> Further, a synthetic fabric manufactured in Israel will not be deemed to be an Israeli product unless the thread used to make it also originates in Israel.<sup>194</sup> There is no doubt that these and other exceptions were created in order to make it more difficult to import products from the other party and to protect local industry.

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<sup>191</sup> 1975 Agreement, *supra* note 173, art. III, Protocol 3, sect. 1(a).

<sup>192</sup> Pursuant to Article 3, section 1 of the 1975 Agreement, the exceptions are set out in "List A" and "List B" in Annexes II and III, respectively, of Protocol 3. In practice, most of Israel's exports fall within these exceptions and not within the rule. 1975 Agreement, *supra* note 173, art. III, sect. 1.

<sup>193</sup> See, e.g., 1975 Agreement, *supra* note 173, List A in Annex II of Protocol 3, Item 61.07; see generally *id.* Items 60-62.

<sup>194</sup> *Id.* Item 51.04. It is necessary that the fabric be manufactured from chemical products or textile pulp, i.e., not just threads.

This is also true of the general prohibition on draw-backs<sup>195</sup> found in the amended Protocol No. 3.<sup>196</sup> Under amended Protocol No. 3, a product manufactured in Israel from raw materials imported from third countries (apart from the EC) and thereafter exported to the EC would not be entitled to a return of the customs duties paid on the raw materials at the time of importation. As a result, its price would rise and it would be more difficult for the product to compete in the European market. The aforementioned provisions, i.e., the strict rules of origin and the prohibition on draw-backs, in practice created hidden trade barriers within the free trade area and thereby limited the effectiveness of the agreement. Indeed, the rules apply to both parties, but it is clear that a small country, such as Israel, which is highly dependent on imported raw materials, will find it more difficult to meet the strict requirements. This has been reflected in Israel's trade deficit with the EC which has soared in the last decade.<sup>197</sup>

#### b. Institutional Deficiencies

The legal deficiency of the 1975 Free Trade agreement becomes even more apparent at the institutional-procedural level. The agreement, in fact, lacks any legal mechanism for dispute settlement be-

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<sup>195</sup> A draw-back is a return or conditional exemption from duties payable on imports of raw materials used for the manufacture of products destined for export. This matter is regulated in Articles 160-162C of Israel's Customs Ordinance (New Version) LSI 1957, p. 39. In the United States, it is regulated in 19 U.S.C. § 1313(a) (1994). See also *United States v. International Paint Co.*, 35 C.C.P.A. 87, 90 (1948) (stating that the underlying goal of the U.S. drawback regulations is to develop and assist U.S. exports).

<sup>196</sup> Article 30 of the amended Protocol No. 3 provides: "Save where decided otherwise by the joint committee, the products referred to in Article 1 of Protocols Nos. 1 and 2, used for manufacture, which do not originate in the EC or Israel, may not be the subject of a return of customs duties or enjoy any exemption from customs whatsoever, commencing on 1 January 1984." This provision applies both to customs duties and charges equivalent to customs duties. In note 7 to this Article (Annex 1 - Explanatory Notes) it is clarified that the prohibition applies "to every provision for the full or partial return or non-collection of customs duties applicable to products used for manufacture, on condition that the aforesaid provision grants, expressly or retroactively, for this return or non-collection, where the goods manufactured from the said products are exported but not where they are destined for national consumption." The prohibition on draw-backs in relation to exports to the EC is implemented in Israel by Article 4(b) of the Customs (Draw-Backs on Goods used to Manufacture Products for Export) Order - 1968, Regulations - 1969, p. 514, as amended.

<sup>197</sup> Whereas in 1975 the trade deficit with the EC stood at US\$784 million, in 1994 it stood at 5,300 million U.S. dollars (according to the figures of the Central Bureau of Statistics). This is not the place to analyze the significance of these figures, but it would appear that the harsh rules of origin contributed to this result. For a comprehensive analysis of the effect of the agreement on Israeli industry, see B. Toren, *The Impact of the FTA with the EEC on Israeli Industry: A Follow-up, in EUROPE AND ISRAEL: TROUBLED NEIGHBOURS* 113 (Greilsammer & J.H.H. Weiler eds., 1988).

tween the two parties or for giving binding interpretations in relation to the provisions of the agreement. The agreement did establish a Joint Committee (which later changed its name to the "Co-operation Council"),<sup>198</sup> whose function was to carry out the agreement "and ensure its proper implementation."<sup>199</sup> However, this was a parity committee which comprised an equal number of representatives from the EC and Israel and whose decisions were made by mutual agreement only.<sup>200</sup> It was, therefore, not possible to bring a dispute or controversy regarding the agreement to an objective independent inquiry. Instead, the agreement adopted the diplomatic model, which, at the time, was common to most trade agreements. A party which believed that the other party had violated the agreement could bring his complaint before the committee through diplomatic channels and attempt to persuade the opposing party of the merits of his claims. He could also threaten unilateral countermeasures. Enforcement of the agreement was built primarily on self-help by means of protective or aggressive retaliation. The agreement only required that, prior to these measures being taken, notice be given to the Joint Committee, sometimes with a cooling-down period, in order to enable the committee to attempt to resolve the dispute peacefully.<sup>201</sup> Where no such resolution was achieved, the injured party became entitled to activate such "protective measures" as appeared to be necessary, including withdrawal of tariff concessions.<sup>202</sup>

There is, of course, a lack of symmetry in the level of effectiveness of a threat to take such measures when it comes from a small country and is directed against a powerful body such as the EC, compared to the opposite situation, and there is no doubt that this state of affairs gives an advantage to the stronger party.<sup>203</sup>

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<sup>198</sup> Additional Protocol to the 1975 Agreement, Sept. 26, 1978, Isr.-E.E.C., Art. 9, 21 O.J. EUR. COMM. (No. L. 270) 4 (1978) [hereinafter Additional Protocol].

<sup>199</sup> 1975 Agreement, *supra* note 173, art. 19:1.

<sup>200</sup> *Id.* art. 20.

<sup>201</sup> *See id.* art. 16. This article provides consultation and hearing procedures in relation to parties' complaints of violations of competition laws (Article 12), increases of imports of specific products in consequence of changes in customs policy of the other side (Article 13 - equalizing charge), imports by dumping (Article 14), and serious interferences in the economy of specific sectors or areas in consequence of the operation of the agreement (Article 15 - safety measures). In all the cases there is a duty of prior consultation with the committee, unless exceptional circumstances require immediate interference (Article 16:3 (D)). *Id.* art. 16(3)(d).

<sup>202</sup> *See, e.g., id.* art. 16(3)(C) (referring to the violation of Article 12). *See also id.* arts. 12-15. *But see id.* art. 16(2) ("In the selection of measures, priority must be given to those which least disturb the functioning of the Agreement.").

<sup>203</sup> *See, for example, the dispute between Holland and the United States in the 1950s, Pescatore, supra* note 98, where Holland waived in advance the imposition of sanctions against the

The next milestone in the history of trade relations between Israel and the EC was the Association Agreement of 1995. However, since this agreement belongs to the "third generation" of FTA agreements, consideration will first be given to "second generation" agreements. Later, we will return to the Association Agreement of 1995.

## B. Israel's Trade Relations with the United States

### 1. *Background to the Signing of the 1985 FTA Agreement*

About a decade after the signing of the FTA agreement with the EC, the State of Israel signed its second FTA agreement, this time with the United States.<sup>204</sup> The decision to negotiate this agreement was reached in November 1983 by President Reagan and Prime Minister Shamir. Israel wished to ensure free access to its second most important export market on a more secure basis than the Generalized System of Preferences (GSP) which had previously applied. The foundations of the GSP had been laid in the GATT<sup>205</sup> and were aimed at aiding developing countries by a unilateral grant of concessions and tariff exemptions on goods imported to the wealthy countries.<sup>206</sup> Israeli exports had enjoyed the benefit of this program for many years. However, Israel feared that export growth would result in forfeiture of its rights and, eventually, loss of its status as a "developing country" in the eyes of the U.S. government.<sup>207</sup>

On the other hand, for the first time in its history, the serious problems encountered in the opening of the Uruguay Round caused the United States to consider an alternative to the multilateral approach embodied in GATT (of which the United States had been the main patron). There were some who hoped that the threat of a bilateral alternative and, in particular, the possibility of establishing a regional trading bloc with Canada, would spur negotiations within

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United States, despite being authorized to impose them by the GATT Council. One may assume that this incident also contributed to Holland's decision to join the EC, which gives its members an organizational framework possessing greater power in the arena of world trade.

<sup>204</sup> Free Trade Agreement, Apr. 22, 1985, Isr.-U.S., 24 I.L.M. 653 (1985) [hereinafter 1985 Agreement].

<sup>205</sup> See GATT, *supra* note 36, art. 34.

<sup>206</sup> See Trade Act of 1974, 19 U.S.C. §§ 1461-65, for the program that was implemented by the United States.

<sup>207</sup> On the background to this agreement, see generally Dennis James Jr., *The Agreement on Establishment of a Free Trade Area Between the Government of the United States and the Government of Israel*, in *THE LEGAL FRAMEWORK FOR CANADA-UNITED STATES TRADE* 121-27 (Maureen Irish & Emily F. Carasco eds., 1987); Susan A. Baldwin, *Recent Developments: International Trade*, 27 HARV. L.J. 289 (1986); Sandra Ward, Note, *The U.S.-Israel Free Trade Area: Is it GATT Legal?*, 19 GEO. WASH. J. INT'L L. & ECON. 199 (1985).

GATT. The FTA agreement with Israel was expected to easily obtain the necessary confirmation in the U.S. Congress where Israel traditionally enjoyed support. Finally, the United States was interested in equating the status of its exports to Israel with that of European exports. As noted previously, the latter were due to obtain a full exemption from customs duties as a result of the FTA agreement with the EC. From the vantage point of the U.S. government, therefore, the agreement with the small and popular State of Israel was regarded as a convenient "experiment" in terms of a first-time FTA agreement. The success of the experiment and the signing of the agreement in the beginning of 1985 allowed the United States to immediately turn its attention to what it regarded as the more significant project—engaging in an FTA agreement with Canada. Such an agreement was signed two years later.<sup>208</sup>

## 2. "Second Generation" FTA Agreements: Substantive Provisions

The FTA agreement with the United States may be defined as a "second generation" FTA agreement, both in substantive terms and at an institutional-procedural level. Like its predecessor, its primary achievement was the elimination of tariffs on the trade between the two countries, a process which was effected over a period of ten years. In contrast to the agreement with the EC, however, under the U.S. FTA agreement, the process was carried out on a reciprocal basis in both countries.<sup>209</sup> Moreover, unlike the EC agreement, the FTA with the United States applies to agricultural products and requires the elimination of all protective tariffs on agricultural goods. Only import restrictions which do not take the form of customs duties, such as quantitative restrictions and special charges, may be imposed by the parties on the basis of agricultural policy considerations.<sup>210</sup> The agreement does not contain a prohibition on customs duty draw-backs, like that which exists in the agreement with the EC. Similarly, the rules of origin in the agreement are not subjected to countless exceptions tailored to meet the protectionist needs of local industry.<sup>211</sup> Further, un-

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<sup>208</sup> The Canada-U.S. Free Trade Agreement, 27 I.L.M. 281 (1988).

<sup>209</sup> See 1985 Agreement, *supra* note 204, art. 2, at 658. The products were divided into groups, each of which was subject to a different timetable for tariff eliminations. See *id.* Annex 2, at 668-69. The final elimination was carried out on January 1, 1995. See *id.* at 669.

<sup>210</sup> *Id.* art. 6. Both Israel and the United States have made use of this authorization and have imposed import quotas on a number of agricultural products. U.S., Israel Agree to Negotiate Greater Access for Farm Products, 12 Int'l Trade Rep. (BNA) 1783 (Oct. 25, 1995).

<sup>211</sup> The rules of origin of the 1985 Agreement are set out in Annex Three of the agreement. See 1985 Agreement, *supra* note 204, Annex 3, at 669-73. These rules are not based on the change of customs classification criteria, but on the "substantial transformation" test, together

like its predecessor, the agreement prohibits quantitative restrictions on exports and applies the general prohibition on new restrictions, such as customs duties, equivalent charges, quantitative restrictions and measures having equivalent effect, on both imports and exports.<sup>212</sup>

The regulation of NTBs under the Israel-U.S. FTA is, therefore, more highly developed than under the 1975 agreement with the EC. Apart from the general prohibition referred to above, the U.S. agreement contains an article prohibiting each party from making imports from the other conditional upon obtaining an import licence. This prohibition is subject to only two exceptions: (1) where the licence is automatically approved (such licenses are generally issued for statistical purposes), or (2) where the licence is necessary in order to administer a quantitative ceiling on imports justified under the FTA or under GATT.<sup>213</sup> The issue of export subsidies is also comprehensively regulated by the agreement. Indeed, upon the request of the United States, Israel undertook in Annex Four of the FTA to accede to the Subsidies Code of GATT.<sup>214</sup> This Code, which was developed during the Tokyo Round,<sup>215</sup> prohibits the grant of export subsidies with respect to all industrial products. The FTA agreement also contains provisions requiring liberalization in government procurements,<sup>216</sup> as well as an undertaking to protect intellectual property rights.<sup>217</sup> In addition, there is a prohibition on the imposition of trade-related performance requirements as a condition for the authorization of investments

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with a demand for added value of 35%. As mentioned previously, there are no exceptions to this general rule, and accordingly there is no room for special requirements designed to prevent or make it more difficult to engage in imports from the other side in "sensitive" sectors. For an extensive discussion of these rules of origin, see Allan S. Galper, Note, *Restructuring Rules of Origin in the U.S.-Israel Free Trade Agreement: Does the EC-Israel Association Agreement Offer an Effective Model?*, 19 *FORDHAM INT'L L. J.* 2028, 2065-67 (1996).

<sup>212</sup> 1985 Agreement, *supra* note 204, art. 4, at 658; Cf. 1975 Agreement, *supra* note 173, arts. 3-4.

<sup>213</sup> 1985 Agreement, *supra* note 204, art. 12, at 661.

<sup>214</sup> See *id.* Annex 4, at 663. Israel also undertook not to institute any new export subsidy programs and not to increase the level of subsidization in existing programs above the level prevailing on November 7, 1984. *Id.* at 673-74. Similarly, Israel undertook to eliminate the subsidy elements from all its export assistance programs. *Id.*

<sup>215</sup> See WTO Agreement, *supra* note 42, Annex IA(6), at 29.

<sup>216</sup> 1985 Trade Agreement, *supra* note 204, art. 15, at 662-63. For an extensive discussion of this provision, see Arie Reich, *Toward Free Trade in the Public Sector: A Comparative Study of International Agreements on Government Procurement* 365-75 (Doctoral Thesis, University of Toronto, 1994) (unpublished and on file with the University of Toronto library).

<sup>217</sup> 1985 Agreement, *supra* note 204, art. 14, at 662.

by nationals of the other party.<sup>218</sup> This provision is in the nature of a preliminary and more limited version of the TRIMs agreement, signed a decade later within the framework of the Uruguay Round.<sup>219</sup>

A further important innovation of the FTA of 1985, which too foreshadowed the Uruguay Round, may be seen in the provisions relating to trade in services. In Article 16, the parties proclaim their recognition of the importance of trade in services and the need to maintain an open system of services exports which would minimize restrictions on the flow of services between the two nations. Apparently, the novelty of this concept led to the provision, being formulated as "soft law," within the framework of a joint declaration annexed to the agreement. The declaration refers to the need to liberalize this area on the basis of three principles: (1) the establishment of a free market for the service industries of both parties; (2) treatment of the service industries of the other party not less favorable than that afforded local firms; and (3) open and accessible information about laws and regulations concerning services.<sup>220</sup>

### 3. *The Supervisory and Dispute Settlement Mechanism*

The supervisory and dispute settlement mechanism contained in the 1985 agreement provides further evidence of the greater degree of sophistication of this agreement. The agreement sets up a Joint Committee whose function is to "supervise the proper implementation of the agreement and review the trade relationship between the Parties."<sup>221</sup> The functions and powers of the Committee are expansively defined, and each party is entitled to demand the convening of the Committee upon giving twenty-one days' notice. The agreement requires each party to give the other party prior written notice before

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<sup>218</sup> *Id.* art. 13, at 662. The article prohibits each side from imposing, as a condition for establishing, expanding or maintaining investments by nationals or companies of the other party, requirements to export any amount of production resulting from such investments or to purchase locally-produced goods and services. *Id.* Moreover, it prohibits the imposition of requirements on investors to purchase locally-produced goods and services as a condition for receiving any type of governmental incentive. It should be noted that export requirements are prohibited solely when they are made a condition to the "establishment, expansion or maintenance of investments," but not when they are imposed as a condition to obtaining government incentives. *Id.* This conclusion arises out of the comparison between the first sentence and the second sentence of the article. It follows that export requirements which occasionally are involved in the award of the status of an "authorized plant" under the 1959 Encouragement of Capital Investments Law, are not prohibited under this agreement. Nevertheless, there is place to examine their legality under the new TRIMs agreement.

<sup>219</sup> WTO Agreement, *supra* note 42, Annex IA, at 29

<sup>220</sup> See James, *supra* note 207, at 126.

<sup>221</sup> 1985 Trade Agreement, *supra* note 204, art. 17(1), at 663.

taking any trade measures with respect to products traded between the two nations. Such notice gives a party affected by these measures a suitable opportunity for consultation.<sup>222</sup> The dispute settlement mechanism of the agreement is set out in Article Nineteen. The grounds for invoking the mechanism are similar to those found in Article XXIV of GATT and include not only an allegation that the agreement (including the Subsidies Code) has been violated,<sup>223</sup> but also a claim that a party considers that "measures taken by the other party severely. . . distort the balance of trade benefits accorded by [the agreement] or substantially undermine fundamental objectives of [the agreement]."<sup>224</sup> The agreement provides for the following procedural stages. First, when a dispute arises, the parties shall make every attempt to arrive at a mutually agreeable resolution through consultation.<sup>225</sup> If this is unsuccessful, either party may then refer the matter to the Joint Committee, which will be convened and will endeavor to resolve the dispute.<sup>226</sup> In the event that the dispute is not resolved by the Committee within a period of sixty days, then either party may refer the matter to a conciliation panel. The conciliation panel is to be composed of three members.<sup>227</sup> The primary task of this panel is to effect a compromise between the parties and to reach an agreed resolution of the dispute. However, if the panel fails to effect a compromise, then the panel will be transformed into an arbitration panel whose function is to hear the claims of the parties and their evidence and to make factual and legal determinations regarding the dispute before it.<sup>228</sup> Similarly, the panel must draft a "proposal" for the settle-

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<sup>222</sup> *Id.* art. 18, at 664.

<sup>223</sup> However, the mechanism may not be invoked in respect of the unilateral imposition of anti-dumping or countervailing duties. *Id.* art. 19(1)(A), at 664-651.

<sup>224</sup> *Id.* There is room to discuss the relationship between this formula and the formula set out in Article XXIV of GATT, which refers on "nullification or impairment of benefits". *Prima facie*, Article 19 is more limited, in that it requires a "serious" distortion of the balance of trade advantages between the two countries. This therefore implies a narrowing of the non-legal grounds of GATT 1947, a change which is compatible with the juridicization process under discussion here.

<sup>225</sup> *Id.* art. 19(1)(b), at 665.

<sup>226</sup> *Id.* art. 19(1)(c), at 665.

<sup>227</sup> *Id.* art. 19(1)(d), at 665. Under this system, the State of Israel will usually appoint an Israeli citizen as an arbitrator on its behalf; the United States will likewise appoint an American citizen as an arbitrator on its behalf. The two arbitrators will jointly appoint a neutral third arbitrator, who is a citizen of a third country. This is what occurred in the *Sharnoa* arbitration. See *infra* note 230 and accompanying text.

<sup>228</sup> 1985 Agreement, *supra* note 204, art. 19(1)(E), AT 665. See also Avraham Azrieli, *Improving Arbitration Under the U.S.-Israel Free Trade Agreement: A Framework for a Middle-East Free Trade Zone*, 67 ST. JOHN'S L. REV. 187, 227 (1993).



ment of the dispute. However, the agreement expressly provides that "[t]he report of the panel shall be non-binding."<sup>229</sup>

This dispute settlement mechanism was successfully invoked by Israel in the "Sharno" affair. In that case, Israel complained that products of an Israeli plant (Sharno), which were recognized as fulfilling the rules of origin requirements of the FTA, were being counted by the U.S. authorities within the export quotas of Taiwan. As a result, the Taiwanese suppliers of Sharno's components stopped supplies to the Israeli company, and Israel was left without a source for these components. The Taiwanese suppliers preferred to export the full quota of completed products to the United States, rather than export components to the plant in Israel. Following Sharno's complaint to the Ministry of Trade and Industry, the State of Israel commenced consultations with the United States to resolve the problem. When the consultations did not succeed, the dispute was referred to the conciliation/arbitration panel.<sup>230</sup> Following a hearing, the panel held, in a well-reasoned opinion extending over forty pages,<sup>231</sup> that the United States had violated the agreement by "counting" the Israeli exports within the Taiwanese quota. The decisive for the panel was the conclusion that the United States' action, in effect, imposed a restriction on Israeli exports to the United States,<sup>232</sup> without one of the qualifications set out in the agreement permitting it to do so. The panel held that the United States was required to stop designating the Israeli

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<sup>229</sup> 1985 Trade Agreement, *supra* note 204, art. 19(1)(e), at 665.

<sup>230</sup> The State of Israel appointed Professor Joseph H. Weiler of the University of Michigan, an expert in E.C. and international trade law, as its arbitrator. The United States appointed Professor Greenwald, a previous U.S. Ambassador to the E.C. institutions, as its arbitrator. These two persons chose Professor Donald MacCrea of Canada, the Dean of the Law School in Ottawa, as the chairman of the arbitration panel. The arbitration took place in Washington in the beginning of 1991. From discussions with officials involved in the process. See also Azrieli, *supra* note 228, at 206.

<sup>231</sup> To date, the arbitration award has still not been formally published because of the strict refusal of the United States to permit publication. This author's application to the U.S. authorities in this regard met with no response. The contents of the award may be read in a variety of newspaper articles and in the press notice of June 17, 1991, published by the legal advisor to the Israeli Ministry of Trade and Industry. See Arbitration Panel says U.S. violated Israel FTA in Attempt to Block Taiwan Machine Tools, *Int'l Trade Rep. (BNA)* (July 17, 1991).

<sup>232</sup> The panel inferred that the United States had violated the provision in Article Four which refers to "equivalent measures" (that is, measures having the equivalent effect to that of quantitative restrictions). This article was apparently interpreted by testing its result, that is, whether the United States was violating that agreement if it did not impose any direct restriction on Israeli products, but the practical result of its actions was that importation of the Israeli products into the United States was nevertheless prevented. This interpretation conforms to the interpretation given by the EC Court to the parallel provision in the Rome Treaty. See *Procureur du Roi v. Dassonville* (1974) ECR 837; [1974] 2 CMLR 436 (E.C.). Since two of the arbitrators were professors of EC law, the similarity in the two interpretations was probably not a coincidence.

product as a Taiwanese product and recommended that the parties consider a compromise solution. Following the panel's decision, a compromise was reached which was satisfactory to Israel.

Therefore, this is a dispute settlement mechanism which is more developed from a legal point of view than the mechanism (or more accurately, the non-existent mechanism) in the 1975 FTA agreement. However, it is less developed than the 1994 binding mechanism of the WTO. In fact, the Israel-U.S. mechanism resembles the system existing at the time in GATT disputes, as reflected in the understanding on dispute settlement drafted during the Tokyo Round in 1979.<sup>233</sup> Not only are the grounds of complaint similar, but both agreements grant the right to refer the dispute to an independent panel of arbitrators and obtain a legal and factual determination with a practical recommendation for a solution. In both agreements, this determination is only a recommendation which, in order for it to be binding, requires the agreement of the parties themselves.<sup>234</sup> One cannot assume that this similarity is coincidental. It is likely that it reflects certain accepted concepts with regard to the manner of settlement of trade disputes between sovereign states — concepts which express the level of development of international trade law at the relevant time. The pure diplomatic model has long been abandoned, but the pure legal model has not yet been achieved. The result is a diplomatic-legal hybrid which characterizes a transition period in the development of the international legal system

### C. Third Generation FTA Agreements

The 1990's have seen the establishment of third generation FTA agreements. The juridicization process of trade relations is also expressed in the bilateral free trade agreements which the State of Israel

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<sup>233</sup> Understanding Regarding Dispute Settlement, *supra* note 91.

<sup>234</sup> While GATT did not expressly state that the determination was not binding, that was the practical effect of the custom; the GATT panel's recommendation was ultimately not adopted. In one respect, the mechanism of the 1985 Agreement was preferable to that of GATT. That is because the FTA Agreement allowed the complainant state to convene the conciliation/arbitration panel and submit to it its entire complaint. In contrast, under GATT, it was necessary to obtain the unanimous consent of the Council in order to convene a panel and draft its terms of reference. Thus, it was possible that an interested party could block the proceedings altogether under the terms of GATT. See GATT, *supra* note 36, pt. B, sect. 3.1. However, in other respects, the GATT mechanism was more sophisticated and better developed than the FTA Agreement. For example, the GATT mechanism contained hearing regulations and it required that all the members of the panel be independent (that is, they could not be a national of the state which was involved in the dispute), and experts in the field of international trade relations. See Understanding Regarding Dispute Settlement, *supra* note 91. There are no such provisions in the Israel-U.S. Free Trade Agreement.

signed during the middle of this decade.<sup>235</sup> The most prominent example of this is the new agreement between Israel and the EC, known as the Association Agreement, which was signed on November 20, 1995.<sup>236</sup>

1. *The Association Agreement of 1995 Between Israel and the EC*

For many years, the State of Israel wished to revise the trade agreement of 1975, some of the flaws of which have been described above. However, frosty political relations between Israel and the EC prevented this from occurring. Israel's trade deficit with the EC grew, and it was feared that the situation would deteriorate even further with the enlargement of the EC, the establishment of the European Economic Area with the EFTA States and the strengthening of ties with the countries of Eastern Europe. The changes anticipated from the Uruguay Round of GATT also necessitated a revision and reconsideration of the agreement. Bilateral relations only started warming up after the Middle East peace process strengthened with the Europe-

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<sup>235</sup> It should be noted that in 1992, the State of Israel signed its third FTA agreement, this time with EFTA. The agreement came into force on January 1, 1993. See EFTA Agrees Free Trade Accord with Israel, REUTER NEWS SERVICE, July 16, 1992, available in LEXIS, Nexis Library, News File. The members of EFTA at the time were: Austria, Norway, Sweden, Switzerland, Iceland, Finland and Lichtenstein. The principal reason for signing this agreement was the establishment of the "European Economic Area" between EFTA states and the EC, which *inter alia* unified tariffs between the two entities. Accordingly, it was necessary to harmonize the relations between Israel and the EFTA States on one hand, and the relations between Israel and the EC on the other. In this agreement there are many provisions which are more sophisticated than those contained in the 1975 agreement with the EC, such as the provisions concerning government procurements, protection of intellectual property rights, a declaration on trade in services and more. However, the potential of these provisions has never been realized, as a short time after this agreement came into force, four of the EFTA states gave notice that they wished to join the EC. Three of them (Sweden, Austria and Finland) have since done so, so that the importance of the agreement has been greatly reduced.

<sup>236</sup> The Euro-Mediterranean Agreement Establishing an Association between the European Communities and their Member States, of the one part, and the State of Israel, of the other part (unpublished) [hereinafter Association Agreement]. At the time of writing, this agreement has not yet been ratified, and accordingly has also not yet been published in the official gazette. However, as the ratification process is expected to be a lengthy one, and in order to obtain immediate implementation of the provisions of the agreement relating to free trade, the parties have signed an Interim Agreement on Trade and Trade Related Matters, which came into force on January 1, 1996. The interim agreement contains, in the main, all the provisions of the Association Agreement relating to the movement of goods, free competition, property rights, customs, the Joint Committee, dispute settlement, annexes and protocols relating to agricultural products, rules of origin and co-operations in customs matters. On the Association Agreement, see Galper, *supra* note 211, at 2084-91; Moshe Hirsh, *The 1995 Agreement Between the European Communities and Israel: Three Unresolved Issues*, 1 EUR. FOREIGN AFF. REV. 87 (1996).

This article considers the Association Agreement only, on the assumption that the ratification process will shortly be completed, and the agreement will thereafter become fully effective.

ans displaying a willingness not only to update the agreement but also to create a completely new international regime.<sup>237</sup> In December 1993, the Council of the European Union authorized the commencement of negotiations, and, after almost two years, the agreement was signed.<sup>238</sup> This agreement is part of the "Euro-Mediterranean Partnership" program, within which the EC intends to sign association agreements with many Mediterranean countries.<sup>239</sup>

a. Substantive Provisions of the Agreement

The new agreement creates a comprehensive and inclusive regime with respect to most areas of international trade and even to many areas which are outside the field of trade. The agreement belongs to the type of associations agreements which are designed to create a close economic relationship between the EC and third countries, a relationship which goes beyond the relations created by ordinary FTAs, but which of course falls short of full membership in the EC.<sup>240</sup>

The agreement reinforces the FTA which was established between the parties in 1975.<sup>241</sup> The implicit permission found in the old FTA to impose quantitative restrictions on exports are annulled by the new agreement. Thus, all quantitative restrictions or measures having equivalent effect, whether on imports or exports, are prohibited.<sup>242</sup> Important amendments have also been made regarding rules of origin,<sup>243</sup> although not all of the changes desired by Israel have

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<sup>237</sup> Galper, *supra* note 211, at 2088-91.

<sup>238</sup> Association Agreement, *supra* note 236.

<sup>239</sup> Agreements similar to that signed by Israel and the EC have also been signed with Morocco and Tunisia. Negotiations are underway with Egypt, Jordan and Lebanon and are also expected with Algeria; preliminary talks are being conducted with Syria. Galper, *supra* note 211, nn.371-72.

<sup>240</sup> On the foreign relations of the EC, *see* LEV, *supra* note 184, at 183-91.

<sup>241</sup> Association Agreement, *supra* note 236, art. 6.

<sup>242</sup> *Id.* arts. 16-17.

<sup>243</sup> *See id.* Protocol No. 4 to the Agreement. Two types of changes have been made: (a) Changes necessitated by technological advances since the signing of the previous agreement; thus, in the area of electronics and chemistry alternative rules of origin have been established which are based on the principle of a high added value (generally 75%), without reference to changes in the classification of the tariff; and (b) Changes which allow greater flexibility in the implementation of the rules; first, there is a general flexibility of 10%, under which an exception to the rule is permitted of up to 10% of the value of the exported product. Thus, for example, a product which, according to the rules, must be a product made solely out of local raw materials, may contain up to 10% imported raw materials. Second, there is territorial flexibility of up to 10% of the value of the product, in terms of which it is possible to process original local materials in another country which is not a party to the agreement, on condition that the value of the processing does not exceed 10% of the value of the finished product, and that the product is

been introduced.<sup>244</sup> The FTA has not yet been extended to agricultural products, and, in that sector, many restrictions continue to apply.<sup>245</sup> Nevertheless, the parties have agreed to gradually implement greater liberalization of their trade in agricultural products.<sup>246</sup>

The agreement also contains more sophisticated provisions with regard to non-tariff barriers. These provisions concern important issues, such as dumping,<sup>247</sup> public procurement,<sup>248</sup> standards,<sup>249</sup> subsidies and competition law.<sup>250</sup> In addition, the agreement reflects a

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returned to the local manufacturer before export. (The export must in any event be carried out directly between Israel and the European Union). The above two flexibilities do not apply to textile products and clothing. It is also important to note that large exporters ("authorized exporters") may be exempt from filing certificates of origin - EUR 1, before receiving the benefits of the agreement; this is a significant administrative improvement. *See id.* art. 23, Protocol No. 4.

<sup>244</sup> Israel has still not received a positive response to its request to receive accumulation rights with other countries in Europe, which are not members of the Union. Thus, Israeli components in finished products which are, for example, exported from Switzerland to the EU, will not enable the Swiss manufacturer to benefit from the duty-free treatment to which he would have been entitled had the components been manufactured in Switzerland. This is despite the fact that both Israel and Switzerland have a free trade agreement with the EC. Accordingly, the Swiss manufacturer will prefer to use components manufactured in the EU and not in Israel. Israel's request for cumulative recognition with Arab countries, so as to enable industrial co-operation to the benefit of the peace process, has also not been accepted. Further, the prohibition on customs drawbacks on exports has not been eliminated. *See id.* art. 16, Protocol No. 4.

<sup>245</sup> For details, *see id.* arts. 10-15 of the Association Agreement. *See also id.* art. 9 (permitting the maintenance of charges on the agricultural component of industrial products).

<sup>246</sup> *Id.* art. 11. From January 1, 2000, the parties will review the situation in order to determine the measures which the EC and Israel will apply as of January 1, 2001, in accordance with this objective.

<sup>247</sup> *See id.* arts. 22, 25:3. These provisions make the anti-dumping procedures subject to the GATT Anti-Dumping Code, but also require that bilateral consultations are conducted concurrently with internal legal proceedings, with the aim of reaching an agreed resolution to the problem.

<sup>248</sup> *See id.* art. 35 which refers to taking measures with a view to a mutual opening of the parties' respective government procurement markets beyond what is required by GATT. This was done after a short period, and two supplementary agreements have been reached in this area, which *inter alia* refer to the important telecommunications sector. The equipment of public plants in this sector (such as Bezeq) will no longer be subject to internal regulations giving preference to local products, where Israeli and EC suppliers respectively are concerned. *See* Proposal for a Council Decision concerning the conclusion of two Agreements between the European Communities and the State of Israel on Procurement by Government and Telecommunications Operations, O.J. EUR. COMM. (No. C162) 10 (1996).

<sup>249</sup> Association Agreement, *supra* note 236, art. 47. This article sets the goal of reducing differences in standardization and conformity assessment. For this purpose the parties shall conclude agreements relating to mutual recognition in the field of conformity assessment, so that standards institutes in all the State parties will be authorized to confirm the conformity to standards of the other country. Negotiations on this issue have already begun.

<sup>250</sup> *Id.* arts. 36-38. In addition to the general provisions taken from Articles 85-86 and Article 92 of the Treaty of Rome (and which were also contained in the old agreement), the Association Agreement provides that the Association Council shall adopt detailed rules for the implementation of these provisions, within 3 years of the agreement coming into force. Such rules are ex-

trend which is characteristic of trade agreements of the 1990's, namely, it touches upon economic areas which are outside the field of traditional trade. Thus, for example, the agreement contains provisions relating to the right of firms of one side to establish themselves in the territory of the other. The agreement also liberalizes the provision of services.<sup>251</sup> There are provisions which are intended to guarantee free movement of capital and payments,<sup>252</sup> as well as protect intellectual property rights.<sup>253</sup> The parties have also agreed to increase cooperation in the area of science and technology.<sup>254</sup> Within the framework of this cooperation, Israel, for the first time, has been allowed to join "the Fourth Framework Program for Research and Technological Development" of the EU. This program is intended to raise the standard of knowledge and the competitive power of industry on the international level by financing development projects and scientific, technological and practical research. The participation of Israel (in return for a sizeable annual membership fee of about \$30 million U.S. dollars) will encourage scientific-technological cooperation between Israeli and European bodies, financed by the program.

The agreement also contains provisions relating to co-operation between the parties on a broad range of other issues, including industry, agriculture, financial services, protection of the environment, energy, information infrastructures and telecommunications, transport, tourism, approximation of laws, drugs and money laundering, migra-

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tremely important for the practical implementation of these provisions. With regard to subsidies, the agreement in the meantime refers to the subsidies agreement of the WTO, discussed above, as binding in respect of the implementation of the prohibition on subsidies. Similarly, there are rules relating to monopolies, which require the parties to ensure that by the end of the fifth year following the entry into force of the agreement, no discrimination regarding the conditions under which goods are procured and marketed shall exist between nationals of the EC and Israel, and that there shall be no other measures distorting the trade between the parties to an extent contrary to the interests of the parties. *Id.* arts. 37-38.

<sup>251</sup> *Id.* art. 29.

<sup>252</sup> *Id.* arts. 31-32. Free movement of capital is one of the "four basic freedoms" guaranteed in the European Common Market. It is anchored in Article 67 of the Treaty of Rome. Treaty of Rome, *supra* note 178. Now, it is also desired to gradually entrench it within the free trade area between Israel and the EC. At the same time Article 33 of the agreement contains a grandfathering provision, under which restrictions which exist on the date of entry into force of the agreement, in respect of the movement of capital between the parties involving direct investment, including in real estate, establishment, the provision of financial services or the admission of securities to capital markets, shall not be prejudiced. In any event, any limitation on repatriation of investments by foreigners is forbidden.

<sup>253</sup> Association Agreement, *supra* note 236, art. 39. According to Annex VII to the agreement, Israel undertakes to accede to a number of multilateral conventions relating to protection of intellectual, industrial and commercial property rights to which the Member States of the EU are party or which they implement in practice.

<sup>254</sup> *Id.* art. 40.

tion policy, the audiovisual sector, education and culture.<sup>255</sup> There are also provisions relating to social matters, such as guaranteeing the rights of workers employed in the other State, and more.<sup>256</sup>

As a rule, the approach adopted by the agreement in numerous areas, particularly in the "new" areas, is the establishment of goals and frameworks for the continued development of the regime. This approach is similar to that occasionally found in the internal legislation of States; primary legislation posits the goals, the basic rules and the authority to promulgate detailed regulations for the achievement of the goals, while these regulations are later settled by secondary legislators who fill the framework with real content.

b. Supervisory and Dispute Settlement Mechanism

Finally, consideration should be given to the institutional provisions of the agreement, which also reflect the greater sophistication of this international trade regime. Here, too, it is evident that the regime bears much resemblance to that found in the multilateral WTO/GATT agreement of the same period.

The agreement establishes an "Association Council" which shall meet at the ministerial level at least once a year.<sup>257</sup> In addition, in order to enable more regular and efficient handling of the numerous matters covered by the agreement, an "Association Committee" is set up which shall consist of officials.<sup>258</sup> The Committee will have the power to make decisions for the management of the agreement, as well as in those areas in which the Association Council has delegated its powers to it. In both these bodies, decisions can be taken by consensus only.<sup>259</sup> However, once the decisions are reached by agreement, they shall be binding on the parties and the parties are required to take the necessary measures to implement the decisions.<sup>260</sup> Contrary to the old agreement with the EC, the new agreement enables the referral of a dispute connected to the application or interpretation of the agreement to arbitration.<sup>261</sup> Contrary to the

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<sup>255</sup> See generally *id.* arts. 45-61.

<sup>256</sup> See *id.* arts. 63-66.

<sup>257</sup> *Id.* art. 67.

<sup>258</sup> *Id.* arts. 70-71.

<sup>259</sup> See *id.* art. 69:2 (regarding the Association Council); see also *id.* art. 72:2 (regarding the Association Committee).

<sup>260</sup> *Id.* arts. 69:1, 72:1.

<sup>261</sup> *Id.* art. 75:4. Such a referral will take place where the Association Council fails to settle the dispute by agreement. In such a case, each party may notify the other of the appointment of an arbitrator; the other party must then appoint a second arbitrator within two months (for this purpose the EC and the Member States are deemed to be one party to the dispute). The Associ-

agreement with the United States, here, the decisions of the arbitrators (which may be reached by a majority vote) are binding.<sup>262</sup>

In addition to the resemblance on this last issue with the WTO dispute settlement mechanism, it is interesting to note similar trends in the stance toward non-legal grounds of complaint under both regimes. It will be recalled that the 1985 FTA with the United States of 1985 recognized grounds for a complaint arising otherwise than by virtue of a violation,<sup>263</sup> as did the GATT agreement of 1949.<sup>264</sup> In contrast, it does not appear that the new agreement with the EC recognizes such grounds of action. Rather, the general relief provided by arbitration and the imposition of sanctions is limited solely to cases of violation of the provisions of the agreement.<sup>265</sup> This development is consistent with the process of juridicization considered in relation to GATT, and in particular the Uruguay Round, which significantly restricted the use of non-legal grounds of action.<sup>266</sup> One must, however, note one significant shortcoming in the new dispute settlement mechanism of the Association Agreement, and that is the absence of an exclusivity and primacy clause, similar to the provision found in the WTO.<sup>267</sup> The referral of a dispute to the Association Council is a right, not an obligation,<sup>268</sup> and the agreement does not seem to pro-

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ation Council will appoint a third arbitrator. Here there is a certain flaw in the procedural provisions relating to the establishment of the panel of arbitrators, as a defending party may *prima facie* suspend his agreement to the appointment of the third arbitrator, or reject every candidate proposed, and thereby block the proceedings, since every decision of the Association Council must be unanimous. In view of this, the parties have issued a joint declaration concerning Article 75 to the effect that "the parties shall endeavor to ensure that the Association Council shall appoint the third arbitrator within 2 months of the appointment of the second arbitrator."

<sup>262</sup> Article 75:4 provides: "Each party to the dispute must take the steps required to implement the decisions of the arbitrators." *Id.* art. 75:4.

<sup>263</sup> Article 19(a) of the 1985 Agreement, *supra* note 204.

<sup>264</sup> See *supra* note 83, and accompanying text.

<sup>265</sup> Article 75 of the agreement provides that it is possible to refer "any dispute relating to the application or interpretation of this agreement" to the Association Council, and thereafter to arbitration. Association Agreement, *supra* note 236, art. 75. There is no reference whatsoever to "nullification or impairment of benefits", or to a "serious distortion of the balance of trade advantages," or "undermining the purposes of the agreement", such as may be found in the other agreements mentioned. Similarly, Article 79:2, which refers to taking counter measures, applies only when it appears to one of the parties that the other party "has failed to fulfil an obligation under the agreement."

<sup>266</sup> The ground of "nullification or impairment of benefits" does still exist, but in cases of "non-violation nullification or impairment of benefits" numerous limitations apply; *inter alia*, there is no longer an obligation to order the revocation of the injurious measure. See *infra* Sect. C, para. 3.2.7. On the other hand, proof of a violation creates a presumption of "nullification or impairment of benefits", so that the cumulative result of these changes is a return to the more legal category of "violation."

<sup>267</sup> The DSU, *supra* note 118, art. 23.

<sup>268</sup> The Association Agreement, *supra* note 236, art. 75:1.



hibit unilateral action not authorized by arbitrators.<sup>269</sup> This may prove to be a problem in the future.

## 2. *Other Third Generation Trade Agreements*

In addition to the new agreement with the EC, the State of Israel is currently negotiating additional trade agreements. For example, negotiations have been advanced with Canada<sup>270</sup> and Turkey, as well as with several East European countries. In many cases, the drafts of the agreements have already been finalized, although they have not been signed or ratified. These agreements, even where they are first-time agreements between Israel and the above countries, also reflect an advanced level of substantive and procedural legal sophistication.<sup>271</sup> They, therefore, support the existence of a process of juridicization, as put forth in this article.

Abundant evidence of this process may also be adduced from bilateral and regional trade agreements entered into by other countries, such as the NAFTA agreement between the United States, Canada and Mexico,<sup>272</sup> trade agreements in South America,<sup>273</sup> European agreements, and more.

## IV. THE CAUSES OF THE JURIDICIZATION PROCESS

How may this phenomenon be explained? Why have governments gradually abandoned the flexible, diplomatic model for regulat-

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<sup>269</sup> On the contrary, art. 79 allows any Party to take "appropriate measures," if it considers that the other Party has failed to fulfill an obligation under the Agreement. While it is required to supply the Association Council with all relevant information, in order to enable the Council to seek an acceptable solution, it is not obliged to wait for such a solution before taking measures.

<sup>270</sup> On August 1, 1996, shortly before the completion of this article, a new FTA was signed between Canada and Israel (not yet published). The FTA has still to be ratified, but is expected to come into force on January 1997, if all procedures are completed. A brief analysis of the agreement shows that it fits very well into the thesis of this article. It establishes a broad and advanced FTA regime in relation to trade in goods, with several innovative and liberalizing provisions with regard to rules of origin (Tolerance, Fungibility, Minor Processing, and Transshipment - see chapter 3). It incorporates many of the "modern" provisions of the GATT, and includes provisions on new areas not yet covered by GATT, such as competition policy (chapter 7). Finally, it features a sophisticated and binding dispute settlement mechanism (chapter 8), based on standards of due process and transparency, which strongly resembles the WTO mechanism in this field.

<sup>271</sup> This analysis is based on conversations conducted by the author with senior government officials involved in the negotiations. As these agreements have still not been completely finalized and have not been published, it is not possible to discuss them more fully here.

<sup>272</sup> Compare North American Free Trade Agreement, Dec. 17, 1992, Can.-Mex.-U.S., 32 I.L.M. 605 (1993), with Free Trade Agreement, Dec. 23, 1987, Can.-U.S., 27 I.L.M. 293 (1988).

<sup>273</sup> See generally Sam Laird, *Latin American Trade Liberalization*, 4 MINN. J. GLOBAL TRADE 195 (1995).

ing trade relations in favor of a stricter, legalistic model? Why are we now witnessing a greater sophistication and expansion of all the international trade regimes, both on the multilateral and bilateral levels?

There are a number of possible answers to these questions.

#### A. "Natural" Evolution

It is possible to argue that the States learned from experience and saw that the flexible model could not guarantee the efficient functioning of the trade regimes, and that their economic interests required the establishment of a distinct and strong regime which could be enforced. Indeed, there are legal schools of thought which hold that norms and legal mechanisms evolve in a manner partially analogous to natural evolution as propounded by Darwin.<sup>274</sup> The norms and mechanisms which serve certain social goals best are the ones which will ultimately be selected and disseminated.

On its own, this approach may, at best, supply a conceptual framework for considering the phenomenon, but it cannot explain its causes. Why is the legal model the preferred model for regulating trade relations in the opinion of the GATT parties? If this is indeed the case, why did they not evolve fifty years ago?

#### B. The Functionalist Theory

Similar to the evolutionary approach is the functionalist theory regarding processes of political integration developed by David Mitrany.<sup>275</sup> According to this theory, modern times have seen the increasing importance of apolitical technical problems, the resolution of which requires international cooperation between "technicians," rather than cooperation between politicians. Mitrany's theory includes the doctrine of "ramification," according to which the development of cooperation in one technical area leads to similar conduct in other technical areas as a result of the need to widen the cooperation and transfer the successes to additional related areas. So far, this theory has been implemented primarily in the context of the integration of

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<sup>274</sup> See LLOYD, *supra* note 9, at 551-52. The leading proponent of this view was Herbert Spencer (1820-1903) who believed that natural evolution was the key to understanding social and legal developments. He regarded this approach as highly scientific, and in his view it justified an attitude of *laissez faire* in all fields of economics as well as severe limitations on governmental interventionism. Today there is renewed interest in this theory. See, e.g., R. Clark, *The Interdisciplinary Study of Legal Evolution*, 90 YALE L. J. 1238 (1981); M.B.W. Sinclair, *Evolution in Law: Second Thoughts*, 71 U. DET. MERCY L. REV. 31 (1993).

<sup>275</sup> See generally D. MITRANY, *A WORKING PEACE SYSTEM* (1966).

the EC.<sup>276</sup> It explains how the integrated regimes expand outwards from the pure field of trade toward policy issues relating to investments, transport, taxation, social policy and monetary policy.

Applying this theory in the context of GATT, it is possible to explain the substantive element of the juridicization process, i.e., the phenomenon of the multiplication of norms and the expansion of the areas regulated within GATT. One may, therefore, argue that, as the process of reciprocal elimination of tariffs under GATT made progress and enjoyed successful results, the problem of NTBs as the major obstacle to international trade liberalization became more evident. Likewise, the more successful the regime was in the area of trade in goods, the greater the need to expand it to trade in services and to deal with trade distortions originating from the protection of intellectual property rights.<sup>277</sup> The next issue of importance, which is akin to the above matters, is undoubtedly investments, and voices are already heard suggesting that this matter be dealt with in the next round of GATT negotiations.<sup>278</sup>

However, it would seem that, on its own, the functionalist theory is incapable of explaining the procedural juridicization process, which has led to the creation of legal mechanisms for enforcing the agreed rules. When a trade dispute arises and there is an open clash between the interests of the States involved, there are often strong domestic and external political interests involved, and the questions go beyond pure "technical" issues. One must therefore consider why, in recent years, States have suddenly agreed to make themselves subject to enforcement procedures which were, in earlier years, completely unacceptable to them.

### C. The Decline of American Hegemony

Numerous scholars have pointed out that many international regimes in the world economy were established and maintained in the period following World War II by virtue of the existence of the clear hegemony of the United States in the world order. The hegemonic power of the United States served as the central force behind the es-

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<sup>276</sup> JAMES E. DOUGHERTY & ROBERT L. PFALZGRAFF, *CONTENDING THEORIES OF INTERNATIONAL RELATIONS* 432 (3rd ed. 1990).

<sup>277</sup> See *supra* Part II, para. B:3.

<sup>278</sup> In the Singapore Ministerial Conference of the WTO, held in December 1996, it was decided to establish a working group "to examine the relationship between trade and investment." Article 20 of The Ministerial Declaration <<http://www.wto.org>>. This was a compromise between the developed countries' demand for negotiations in this field and the opposition of the developing countries.

tablishment of these regimes.<sup>279</sup> Examples are provided by all the Bretton Woods institutions, including GATT, which were integrated into the *Pax Americana* of the 1940's. Nevertheless, as Professor Keohane has shown, these regimes may continue to flourish on the basis of more equal cooperation between the States, even after the decline of American hegemony, by virtue of the joint interest of all parties in their continued existence.<sup>280</sup> Utilizing game theory and the Coase theorem,<sup>281</sup> Keohane explains how these regimes reduce the transaction cost involved in achieving agreements and cooperation between the States and raise the costs of violating them.<sup>282</sup> This result is achieved by the transformation of the parties into "repeat players" and intertwining different reciprocal interests which are subject to one regime. Thus, a measure which harms a certain State is no longer a one-time action *per se* without general significance but is, rather, a violation of GATT with significant repercussions on a wide number of issues and interests of the violating State. The temptation to "cheat" declines, whereas the value of reputation rises. In this way, the regime succeeds in anchoring the mutual expectations of the parties on stable foundations and in reducing the uncertainties of international trade. Similarly, it reduces the costs involved in achieving new Pareto-optimal transactions between the States, since the forum and framework already exist and the rules of the game are known.

This line of thought leads to the following possible explanation. During the period of American hegemony, which lasted until the end of the 1960's, there was no need for a strong enforcement procedure and an expansive regime. The power of American influence came *in lieu* thereof, and it ensured that the contracting parties of GATT would also honor their commitments for the benefit of the regimes established by it. Indeed, when the United States itself was not inter-

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<sup>279</sup> Robert Gilpin has put it thus: "the Pax Britannica and Pax Americana, like the Pax Romana, ensured an international system of relative peace and security. Great Britain and the United States created and enforced the rules of a liberal international economic order." ROBERT GILPIN, *WAR AND CHANGE IN WORLD POLITICS* 145 (1981). See also CHARLES P. KINDLEBERGER, *THE WORLD IN DEPRESSION: 1929-1939* 305 (1973).

<sup>280</sup> See generally ROBERT E. KEOHANE, *AFTER HEGEMONY: COOPERATION AND DISCORD IN INTERNATIONAL ECONOMIC RELATIONS* (1984).

<sup>281</sup> This theorem was first formulated in Ronald Coase, *The Problem of Social Cost*, 3 J. L. AND ECON. 1 (1960). The theorem states that a Pareto-optimal corrective transaction can only be ensured under three conditions: a legal system which determines liability for actions and which may be enforced by the State; full information; and zero transaction costs. Keohane concludes from this that the creation of a regime which determines clear rules of liability and supplies information at a low cost to all the parties, will inevitably assist in achieving efficient solutions which are based on co-operation between the parties. KEOHANE, *supra* note 280, at 87.

<sup>282</sup> KEOHANE, *supra* note 280, at 85-109.

ested in the promotion of the regime in a particular area, the regime was not established in that area. Thus, for example, the establishment of the International Trade Organization was torpedoed by the United States Senate. Similarly, in the 1950's, agricultural regulation collapsed completely as a result of being abandoned by the United States.<sup>283</sup> With the decline of the United States hegemony in the 1970's and the rise in power of new economic centers, such as the EC, Japan, Canada and, recently, other Far East countries, including Taiwan, Korea and China, there was a greater need for a strong and autonomous regime with effective and independent enforcement mechanisms. It is interesting that in this period it was actually the United States that utilized the GATT dispute settlement procedures more than any other country.<sup>284</sup> Accordingly, it was also the United States which was the principal advocate of strengthening the GATT enforcement mechanism, whereas the other parties ultimately preferred that mechanism to the unilateral retaliatory measures which the United States could adopt under the notorious Section 301.<sup>285</sup>

On this basis, it is also possible to explain the phenomenon of the expansion of the GATT regime to new areas, such as services and intellectual property.<sup>286</sup> Because of the decline of American hegemony, there was a growing need to base the regime on a wider consensus of mutual benefits. For this purpose, it is necessary to identify suitable "exchange transactions" which will be beneficial to all those involved, and, in particular, which will be able to bridge the adverse interests of the developed States *viz a vis* the developing States. Expanding the application of the agreement to a greater number of areas will naturally increase the scope for identifying such transactions.

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<sup>283</sup> JOHN. H. JACKSON, *WORLD TRADE AND THE LAW OF GATT* 718 (1969).

<sup>284</sup> Between the years 1948-1989, the United States filed 71 official complaints within the GATT framework, with only a small percentage of complaints being filed before the 1970s. The European Community, which is next in line, filed only 30 complaints and even if the individual complaints of the States comprising the EC are added to this figure, the total does not match the number of complaints filed by the United States. (It is noteworthy that Japan filed only 4 complaints during this entire period). HUDEC, *supra* note 4, at 395-404.

<sup>285</sup> See CROOME, *supra* note 41, at 279. In contrast to this analysis, compare the contrary assessment made in 1991 (which ultimately proved to be mistaken) to the effect that "GATT died" because of the impossibility of maintaining such a system with the hegemonic power of the United States. Lester C. Thurow, *GATT is Dead*, *JOURNAL OF ACCOUNTANCY*, Feb. 1991. This article was written during the period of crisis in negotiations in late 1990, with the failure of the Ministerial Committee in Brussels.

<sup>286</sup> It should be pointed out that there are already initiatives on the part of the EC and the United States to commence negotiations to expand GATT to such important new matters as investments, workers' rights, and fair competition rules.

Thus, for example, in the Uruguay Round, the developed countries<sup>287</sup> finally agreed to reduce protective measures for the agriculture and textile industries and open them to imports from the developing countries. This agreement could be reached only by virtue of the consent of the developing countries to sign agreements in the fields of services and intellectual property, where the developed countries see great potential for trade.<sup>288</sup> There are also examples outside the North-South equation. Contrary to the position taken by the United States, France achieved protection for "geographical indications" within the framework of the TRIPs agreement<sup>289</sup> for the benefit of such well-known products as champagne and cognac.<sup>290</sup> The French, however, had to agree to reduce subsidies on agriculture. The fact that the final agreement was part of a "package deal" (or, according to GATT jargon, a "single undertaking"), which comprised many and varied components, was what finally enabled its successful completion.

#### D. The Declining Importance of the Security Factor

Another phenomenon which characterizes the period since World War II, and which has occurred concurrently with the juridicization process, is the gradual process of normalization in relations between the non-communist States (such as the GATT contracting parties), the strengthening of peaceful ties, and the declining fear of military attack by one of these States against another. Over the years, the advanced

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<sup>287</sup> With regard to agriculture, this was true primarily for Japan and the European States, which followed a highly protectionist policy in this area and opposed liberalization, whereas the United States was one of the countries which urged the elimination of the protective measures and subsidies.

<sup>288</sup> See CROOME, *supra* note 41, at 254-55.

<sup>289</sup> See TRIPs Agreement, *supra* note 75, arts. 22-24. "Geographical indications" are terms or other indications which identify the product with a specific geographical source—such as a certain State or region within the State having a reputation in respect of quality or special characteristics. The agreement requires the GATT contracting states to supply internal legal measures to a party interested in preventing the presentation of a product as a product manufactured or produced in a geographical area other than its true place of origin. With regard to wines and alcoholic beverages, such as "champagne" and "cognac" which are in fact names of places in France possessing a reputation in the production of these prestigious beverages, these provisions apply even where the word "like" or "imitation" is added to the term. Thus, it is prohibited to sell Israeli sparkling wine, for example, under the name "champagne like wine," etc.

<sup>290</sup> See Jim Chen, *A Sober Look at Appellations of Origin: How the United States will Crash France's Wine and Cheese Party*, 5 MINN. J. GLOBAL TRADE 29, 55 (1996), which emphasizes that the United States had no interest in acceding to the agreement related to the protection of appellations of origins, and that its accession was solely the result of the agreement being part of the GATT package deal. Nevertheless, the author is not convinced that the TRIPs agreement will give the French the protection they seek. See generally Louis Lorvellec, *You've Got to Fight for Your Right to Party: A Response to Professor Jim Chen*, 5 MINN. J. GLOBAL TRADE 65 (1996) (responding to Jim Chen's article).

democracies have been transformed into prosperous States, less oriented towards military might and more oriented towards economic growth and social security.<sup>291</sup>

How does this development affect the nature of trade relations between these countries? First, security concerns lead to the need to ensure independence from external sources of supply. To guarantee the survival of domestic suppliers with comparative disadvantage, trade protection may be required. Countries with serious security concerns may therefore be reluctant to take upon themselves international obligations which may limit their freedom of action in this regard.<sup>292</sup>

Another explanation is based on the distinction between absolute and relative gains from trade. There is widespread agreement that free trade is beneficial to the economies of all participating countries. Nevertheless, trade does not necessarily benefit all the States to the same extent; it is certainly possible that State A might gain greater benefit than State B. In a situation where there is concern for national security, a State must not only ensure that its absolute gain is maximized, but also that its relative position compared to its neighbors is maximized. Increasing economic disparity between two States might create a strategic threat for the future.<sup>293</sup> Accordingly, it is possible that State B may prefer "managed" trade over free trade and a weak trade regime which would allow the State to conduct managed trade. On the other hand, when this consideration becomes less important, States gain greater freedom to strengthen the cooperation amongst themselves in order to ensure their mutual economic growth and improve the standard of living of their citizens.<sup>294</sup> To this end, a strong and predictable regime is needed.

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<sup>291</sup> See MITRANY, *supra* note 275, at 41-42, 95-96, 136-137, 144-145. See also Edward S. Morse, *The Transformation of Foreign Policies*, 22 *WORLD POLITICS* 371, 383-85 (1970); ROBERT O. KEOHANE & JOSEPH S. NYE, JR., *POWER AND INTERDEPENDENCE: WORLD POLITICS IN TRANSITION* 227 (1977).

<sup>292</sup> Although all international trade agreements include exception provisions for such cases, see, e.g., GATT, *supra* note 36, art. XXI, these provisions may not be broad enough for countries with serious security concerns, and they may also be reluctant to subject themselves to the decision of international tribunals in this regard.

<sup>293</sup> See Joseph M. Grieco, *Anarchy and the Limits of Co-operation: A Realist Critique of the Newest Liberal Institutionalism*, 42 *INT'L ORG.* 485, 487 (1988).

<sup>294</sup> *Id.* at 490. See also Ernst B. Haas, *Technology, Pluralism, and the New Europe*, in JOSEPH S. NYE, JR., *INTERNATIONAL REGIONALISM* 149, 158 (1968) (stating that "the argument is no longer over the slice of the pie to go to each; it is increasingly over the means for increasing the overall size of the pastry").

This explanation offers greater clarification of the linkage between peace, trust and trade relations. In this light, one may also understand why, so long as the Soviet superpower and its satellites in Eastern Europe were perceived to be a strategic threat to the United States and Western European countries which controlled GATT, there was no room on the geopolitical level for the accession of the former States to the GATT framework.<sup>295</sup> Instead, these States established a competing trade organization known as the Council for Mutual Economic Assistance (CMEA).<sup>296</sup>

### E. The Influence of Ideological Changes

Recent decades have witnessed the increasing prominence of liberal-economic ideas among intellectuals, politicians and constituencies.<sup>297</sup> Contemporaneously, socialist and communist regimes are collapsing one after another, along with their underlying ideologies. Appreciation of the benefits of a free economy, open to competition from within and without is spreading along with the recognition of the damage caused by protectionist trade policies. Consequently, it is only reasonable to expect the strengthening of trade regimes based on liberal economic ideas, both institutionally and substantively. It is easier today than in the past to "sell" this type of regime to governments and members of parliament, as well as to members of the business community.

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<sup>295</sup> Another reason was, of course, the fundamental difference between the communist economic system which was built on a government monopoly over trade and the capitalist system which is based on free market forces. The GATT agreement is based on the assumption that in the absence of government trade barriers, private market forces will be able to act on the basis of commercial considerations alone.

<sup>296</sup> This organization was established by the Soviet Union, Bulgaria, Hungary, Poland, Czechoslovakia and Romania in 1949, contemporaneously with the establishment of GATT. In 1950, Albania and East Germany joined; in 1962, Mongolia; in 1972, Cuba and in 1978, Vietnam. Other socialist countries have observer status in the organization. See IVAN SZASZ, *THE CMEA UNIFORM LAW FOR INTERNATIONAL SALES* 33 n.68 (2nd. ed. 1985).

<sup>297</sup> For documentation of the process, see Francis Fukuyama, *The End of History?*, 16 NAT'L INTEREST 3 (1989), and FRANCIS FUKUYAMA, *THE END OF HISTORY AND THE LAST MAN* 42 (1992), where Fukuyama declares the ultimate victory of liberal ideology: "Privatization and free trade have become the new watchwords in place of nationalization and import substitution. . . . As mankind approaches the end of the millenium, the twin crises of authoritarianism and social central planning have left only one competitor standing in the ring as an ideology of potentially universal validity: liberal democracy, the doctrine of individual freedom and popular sovereignty."



F. The Increase of Economic Interdependence of States

Without derogating from the importance of the other factors, it appears that the most important cause of the juridicization process in international trade is the increasing economic interdependence of States. This is one of the most prominent characteristics of world economic developments in recent decades<sup>298</sup> and, undoubtedly, has direct ramifications for the trade policy of all States.<sup>299</sup> As a result of technological developments in recent decades, modes of transport and communication between States have improved unrecognizably. The time and cost needed for the transport of goods have been greatly reduced, and channels of electronic communication enable the instantaneous ordering of goods and transmission of payments. A sharp rise is taking place in the mobility of all economic resources, starting with merchandise, services and capital and ending with technology and manpower, which, in the absence of government intervention, could flow freely between countries. Thus, for example, international trade in merchandise has multiplied twelve-fold since the 1940's, many times more than the world rise in gross national product.<sup>300</sup> In many countries, including Israel, more than fifty percent of GNP originates from international trade.<sup>301</sup> As a result, the economic state of the country is highly dependent on what is done in foreign lands. On the one hand, the interdependence of States has brought about great prosperity and a rise in the standard of living because merchandise is manufactured in the most cost-effective States, utilizing their comparative advantages, and increased competition improves choice and quality and lowers prices. On the other hand, it has become more difficult for national governments to control their own economies and implement economic programs independently, since critical elements such as interest rates and export and import performances are dependent on numerous foreign factors which are outside the governments' control.<sup>302</sup> For example, even an economic superpower such as the

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<sup>298</sup> Cf. MITRANY, *supra* note 275, at 131-37; Haas, *supra* note 294, at 161-62; KEOHANE & NYE, *supra* note 291, at 228.

<sup>299</sup> See also JACKSON, *supra* note 3, at 3, who quotes Martin Feldstein, one-time senior advisor to the American Administration, who wrote in 1985: "The experience of the past few years has underlined the interdependence of the world economy. Sharp changes in international trade, in capital flows and in exchange rates have affected all major economies. The rise in real interest rates everywhere reflects the close link among capital markets."

<sup>300</sup> The value of merchandise trade rose from about \$57 billion in 1947 to \$3,500 billion in 1991. GATT, INTERNATIONAL TRADE 1983/84 (1984); GATT, INTERNATIONAL TRADE 1990/91 (1991).

<sup>301</sup> The OECD Member Countries, 145 OECD OBSERVER 17, 22-23 (1987).

<sup>302</sup> JACKSON, *supra* note 3, at 2-3; see also 1992 A.S.I.L. PROC. 69 (Jackson's statements).

United States appears to be dependent on the automobile marketing policy applied in Japan, and changes in this sector have ramifications for the rate of the dollar and unemployment levels in the United States.<sup>303</sup>

In such a situation, supreme importance is attached to establishing a strong and broadly based world trade regime which will ensure coordination of policies and cooperation on the basis of stability and certainty.<sup>304</sup> Stability and certainty are of critical importance in international trade as the trade system itself is anarchic. The trade system is characterized by the absence of a central government where the States are sovereign. In the absence of legal restriction, the States will endeavour to promote their own immediate interests.<sup>305</sup> On the other hand, clear norms and strong enforcement procedures increase certainty and, by means of a system of sanctions in case of violations, reduce to a minimum the steps which can be taken by foreign governments which are injurious to other States. Such a regime also helps to overcome internal political market failures, which lead politicians to prefer welfare-reducing short-term gains over long-term benefits and stability.<sup>306</sup> Politicians may rely on international obligations in order to overcome internal pressures for trade protection, and, in that sense, the WTO regime serves as an international constitutional restraint on the abuse of foreign policy powers.<sup>307</sup>

In conclusion, the more the world is transformed into a "small global village," the greater is its need for "municipal by-laws" and "local courts" which will regulate its affairs.

## V. ANALOGUES TO THE EVOLUTION OF LAW IN HUMAN SOCIETY

### A. The Origin of Law According to Hobbes

So far this article has dealt with the process of formation of a substantive and procedural legal system which regulates the mutual

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<sup>303</sup> See *supra* note 50 and accompanying text.

<sup>304</sup> Historical testimony as to the influence of this consideration on the support of the EC for the strengthening of the GATT regime, may be found in the statements of Christopher Bail, who was the advisor to the President of the European Commission, Jacques Delors, in the beginning of the 1990s, as well as the legal advisor to the EC Delegation to GATT between 1985-1991, the years during which the Uruguay Round agreement was being prepared. See A.S.I.L. PROC., *supra* note 302, at 74.

<sup>305</sup> See WINHAM, *supra* note 29, at 23; see also HEDLEY BULL, *THE ANARCHICAL SOCIETY: A STUDY OF ORDER IN WORLD POLITICS* (1977).

<sup>306</sup> See TREBILCOCK, *supra* note 26, and accompanying text.

<sup>307</sup> See E.U. Petersmann, *Why Do Governments Need the Uruguay Round Agreements, NAFTA and the EEA?* 1994 AUSSENWIRTSCHAFT 31.

rights and obligations of sovereign States within the field of international trade relations. Nevertheless, it is natural to seek analogues between this process and its possible causes and what we know about the formation of legal systems in general and, in particular, systems which regulate the mutual relations of individuals.

This comparison is particularly appropriate under the Hobbesian theory of the origin of law, a theory whose starting point is the "natural" state of anarchy of "man eat man," which is remedied by means of the "social charter."<sup>308</sup> Contrary to the "natural condition" in Hobbes' writings, which refers to no more than a hypothetical situation which may or may not have existed in the distant past, in inter-State trade relations, the anarchic condition is a very tangible reality, a fact which was undoubtedly appreciated by the officials and statesmen who brought about the GATT agreements. This state of affairs existed, *inter alia*, in the 1930's during the recession when the international trade system collapsed completely, and the attempt to establish even minimal cooperation within the framework of the Geneva Convention on the Restrictions of Imports and Exports in 1927, the work of that year's World Economic Committee, failed.<sup>309</sup> This collapse led to a drastic increase in protectionist measures on the part of all the Western countries, including England. As a result, world trade between the years 1929-1939 was reduced by about sixty-six percent, and the world sank into a deep economic recession.<sup>310</sup> The danger of another similar collapse has never actually passed, and of particular importance was the serious crisis in negotiations during the Uruguay Round in 1990<sup>311</sup> when it appeared to many that the world trade system was on the verge of disintegration.<sup>312</sup> Against this background, the achievement of the "social charter," in the form of the WTO

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<sup>308</sup> THOMAS HOBBS, *LEVIATHAN* (1651). See also LLOYD, *supra* note 9, at 116-17. *Inter alia*, Hobbes expressly refers there to the influence of the anarchy of the "natural condition" on the economy and on international trade, because of the problem of uncertainty: "In such condition, there is no place for Industry; because the fruit thereof is uncertain: and consequently no Culture of the Earth; no Navigation, nor use of the commodities that may be imported by sea. . . and which is worst of all, continuall feare, and danger of violent death; And the life of man, solitary, poore, nasty, brutish, and short. . ." *Id.* at 156 (emphasis added). It is clear that the positivist theory of Austin, to the effect that law is "the command of the sovereign", provides a less comfortable basis for comparison with public international trade law, which is entirely the fruit of conventions and understandings between States and not of norms issued by a supreme legislator—who does not exist.

<sup>309</sup> For a detailed description, see WINHAM, *supra* note 29, at 26-27.

<sup>310</sup> *Id.* at 30.

<sup>311</sup> See CROOME, *supra* note 41, at 275-84.

<sup>312</sup> See Thurow, *supra* note 285; see also BHAGWATI, *supra* note 160; cf. WINHAM, *supra* note 29, at 107-17.

Agreement, prevented the outbreak of anarchy. The States could be said to have created a new legal world trade regime which possessed roots and characteristics similar to EVERY legal system in human society according to the views of such great thinkers as Hobbes, Rousseau and Grotius.<sup>313</sup>

At first glance, the analogy to Hobbes' theory does not seem fully applicable, as Hobbes uses the concept of the social charter to justify totalitarian government.<sup>314</sup> This is borne out of the unconditional duty of the citizens to obey the ruler and place their security and well-being in his hands, in contrast to the international arena of GATT where there is no sovereign other than the States. Instead, particularly in the post-hegemonic period, the actual model is one of cooperation between sovereign States within the framework of an agreed regime and subject to that regime and not to a supra-national body. However, in the more ambitious regime of the EC, which too was founded on the principles of trade liberalization and economic integration and which to a certain extent was a source of inspiration for GATT,<sup>315</sup> the Member States chose a type of Hobbesian model of transferring sovereignty in certain areas to a supra-national governing body, while undertaking to obey its authority.<sup>316</sup> Indeed, there are some who regard the WTO, together with its enforcement mechanisms and decision-making procedures, as the harbinger of "supra-nationalism,"<sup>317</sup> even though the difference between the WTO and the EC (even in its original version before the Maastricht Treaty) are enormous.

## B. The Evolution of Law According to Anthropological Studies

Turning to anthropological studies in relation to the evolution of law in primitive societies, one again finds interesting analogues to the processes which have affected international trade law and the causes

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<sup>313</sup> See LLOYD, *supra* note 9, at 115-17; see also HAIM H. COHEN, *THE LAW* 35 (1992). Of the same generation as Hobbes, Grotius was the greatest originator of international law, and he constructed his philosophy, *inter alia*, on the basis of the theory of the social charter.

<sup>314</sup> In fact, later thinkers used Hobbes' assumptions in order to support a liberal and democratic government. See GEORGE W. PATON, *A TEXTBOOK OF JURISPRUDENCE* 107-08 (4th ed. 1972).

<sup>315</sup> One example of this is the liberalization of trade in services. Another example is the opening of government markets to international competition. See Reich, *supra* note 216.

<sup>316</sup> See TREBILCOCK & HOWSE, *supra* note 14, at 49.

<sup>317</sup> Ralph Nader & Lori Wallach, GATT, NAFTA and the Subversion of the Democratic Process, at 3 (unpublished article on file with author).

thereof, as discussed above.<sup>318</sup> For example, researchers have found a clear correlation between the level of economic development of a particular society and the level of development of its legal institutions.<sup>319</sup> The researchers also point to the interaction and interdependence of different elements of society, a factor which is referred to above in the context of GATT<sup>320</sup> as leading to the development and greater sophistication of the legal system.<sup>321</sup>

Other researchers have pointed to this factor as the reason for the repeal of the right to self-help and the replacement of that right by independent judicial and enforcement systems.<sup>322</sup> As in the GATT framework, the principle of reciprocal duties to which the members of the community are subject and the expectation that this principle be applied have been found to lie at the basis of every primitive legal system.<sup>323</sup> Prior to the creation of efficient judicial and enforcement institutions, enforcement in such a legal system relies on the self-help of the victim acting with the consent or encouragement of society. The more the system develops and central government strengthens, the more the right to self-help is restricted and becomes subject to legal review on the part of the sovereign. Ultimately, it is eliminated altogether.<sup>324</sup> Serious violations, which injure the fabric of society, are

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<sup>318</sup> The comparison between law in primitive societies and public international law is not new. Even Paton, in his book on jurisprudence, refers to the development of primitive law and considers it appropriate to draw an analogy between this and public international law "today." PATON, *supra* note 314. This analogy also underlies Barkun's thesis. MICHAEL BARKUN, *LAW WITHOUT SANCTIONS: ORDER IN PRIMITIVE SOCIETIES AND THE WORLD COMMUNITIES* (1968). See also E. ADAMSON HOEBEL, *THE LAW OF PRIMITIVE MAN: A STUDY IN COMPARATIVE LEGAL DYNAMICS* 331-32 (1967). This point of view perceives the international arena as a community of sovereign States which live together and which require the regulation of the interaction between them in the absence of a sovereign, in exactly the same way as individuals in a primitive, pre-autocratic, society. The absence of legislative authorities and central enforcement, and the "primal" nature of international law as a whole, provide the inspiration for this type of comparison.

<sup>319</sup> A particularly thorough study collated immense quantities of information in respect of more than 400 different tribes, and found that most of the societies in advanced stages of economic development also possess developed legal systems. L.T. HOBHOUSE ET AL., *THE MATERIAL CULTURE AND SOCIAL INSTITUTIONS OF THE SIMPLER PEOPLES* (1915), cited in PATON, *supra* note 314, at 47.

<sup>320</sup> See *infra* Part IV.

<sup>321</sup> See LUCY MAIR, *AN INTRODUCTION TO SOCIAL ANTHROPOLOGY* 141 (2nd ed. 1972), relying on the study undertaken by Prof. Bronislaw Malinowski, *infra* note 323. See also HOEBEL, *supra* note 318, at 316.

<sup>322</sup> See MAIR, *supra* note 321, at 148.

<sup>323</sup> BRONISLAW MALINOWSKI, *CRIME AND CUSTOM IN SAVAGE SOCIETY* 67-68 (1932); and in his introduction to HERBERT IAN HOGGIN, *LAW AND ORDER IN POLYNESIA* xxxvi, xl(1972). See also PATON, *supra* note 314, at 49.

<sup>324</sup> HOGGIN, *supra* note 323, at 230.

punished by excommunication and expulsion from the community.<sup>325</sup> Even after the establishment of courts for the settlement of disputes, the enforcement measures applied by them are primitive. Under Roman law, for example, the plaintiff himself was required to ensure the appearance of the defendant.<sup>326</sup>

As has been seen above, international trade law too is largely based on self-help on the part of the States, i.e., unilateral sanctions against violations injurious to them. This formula is evident particularly in "first-generation" free trade agreements, such as the agreement between Israel and the EC of 1975.<sup>327</sup> That agreement contains no procedure at all for making an objective, independent determination in relation to a dispute arising between the parties, even where the violation is clear. Instead, enforcement is completely dependent on unilateral "defensive steps," i.e., self-help on the part of the State which has been affected.<sup>328</sup> As we have seen,<sup>329</sup> prior to the completion of the Uruguay Round, GATT allowed an objective dispute settlement procedure to be conducted, but also required a significant level of cooperation on the part of the defendant State in order to allow the procedure to go ahead. Its consent was required to the adoption of a panel decision, as well as to its enforcement. An effective, sophisticated and binding dispute settlement mechanism was introduced only in the latest round of talks, but even there the enforcement measures in the event of disobedience continue to be based on self-help with the consent of the "community" (the States of the organization).<sup>330</sup> If the law of international trade will evolve in the manner of ancient law, the future will witness a gradual lessening of the right to self-help and its replacement by sanctions on the part of the "community," i.e., the organization. Such a process is already taking place today within the framework of the EC.<sup>331</sup>

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<sup>325</sup> PATON, *supra* note 314, at 49-50.

<sup>326</sup> See HERBERT FELIX JOLOWICZ, *HISTORICAL INTRODUCTION TO THE STUDY OF ROMAN LAW* 175 (1932). See also PATON, *supra* note 314, at 50-51.

<sup>327</sup> 1975 Agreement, *supra* note 173, at 1-3.

<sup>328</sup> *Id.* arts. 16, 25, at 5-8.

<sup>329</sup> See *supra* Part II.C.1.

<sup>330</sup> See *supra* Part II.C.2.h.

<sup>331</sup> From the beginning, the European Community has possessed supra-national prosecutory and judicial authorities. The European Commission was granted authority by the Treaty of Rome of 1957, *supra* note 178 (the Treaty which established the EEC) to supervise the implementation of the provisions of the Treaty, including filing claims against States which do not fulfill their obligations. *Id.* art. 169. The claims are filed in the European Court of Justice, which too is a supra-national body. However, up to the signing of the Maastricht Treaty in 1992 (the European Union Convention), the Court did not have independent enforcement powers against States, and at the most could declare that a Member State had not fulfilled its obligations. *Id.*

Another interesting analogy concerns the character of the substantive law. It appears that primitive systems of law (and this is also true of English law in the 13th century) are characterized by flexible and lenient rules. Only after long development have the rules become stricter and the drafting more decisive and occasionally formalistic.<sup>332</sup> A process similar to this has been seen in the developmental stages of GATT, as discussed above.<sup>333</sup>

Perhaps the most important lesson to be learned from anthropological studies is that most of the laws of ancient societies reflect some sort of logical-biological reality or functional and important social-economic purpose.<sup>334</sup> This is particularly true of laws which develop over a period of many years and which, therefore, express and serve the needs of the community. Accordingly, compliance with these laws is obtained not only by threat of sanctions in the event of violation, but also, and primarily, by virtue of the recognition among the members of the community of the inherent benefits derived from obedience to laws and the legal system as a whole.<sup>335</sup> This recognition was, undoubtedly, also the decisive factor in the GATT world trade regime, and it explains, more than the fear of sanctions, the fundamental willingness of States to obey this regime, even where in the short term this may entail a conflict with certain national interests.<sup>336</sup> This is borne out by the relatively small number of cases in which there has been a need for sanctions in order to enforce clear norms of the GATT regime. It should not be concluded from this that there is no need for sanctions at all. It is important that sanctions be available and be "put in writing" in case of need. But more important is the ability to achieve a clear and objective determination of the contents and significance of international norms of conduct, on the assumption

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art. 171. The Maastricht Treaty, amended Article 171, and conferred on the Court power to fine a State which refuses to abide by the decision of the Court. See Treaty on European Union, 1992 O.J. (C224) 1, 61-62. See also LEV, *supra* note 184, at 48-49. The fines may be collected by means of deductions from allocations payable to the State from the Community budget. *Id.*

<sup>332</sup> See FREDERICK POLLOCK & FREDERICK WILLIAM MAITLAND, *THE HISTORY OF ENGLISH LAW BEFORE THE TIME OF EDWARD I* 27 (2nd ed. 1899). See also PATON, *supra* note 314, at 53-54.

<sup>333</sup> See *supra* Parts II.B.1-B.2.

<sup>334</sup> MALINOVSKI, *supra* note 323.

<sup>335</sup> The classical expression of this position is, of course, found in the words of Socrates in prison, when his friend tried to persuade him to escape and thereby save his life. See Crito, in *THE COLLECTED DIALOGUES OF PLATO* 27 (Edith Hamilton & Huntington Cairns eds. & Hugh Tredennick trans., 1982).

<sup>336</sup> See JACKSON, *supra* note 3, at 83. See also LOUIS HENKIN, *HOW NATIONS BEHAVE: LAW AND FOREIGN POLICY* 49-68 (2d ed. 1979) (analyzing why States generally obey international law).

that States generally respect the rule *Pacta sunt servanda*<sup>337</sup> and are interested in the proper functioning of the world trade regime.<sup>338</sup>

## VI. CONCLUSIONS

In this article, I have documented the process of juridicization of international trade relations within the framework of GATT and have attempted to explain its causes. This process, particularly as reflected in its most recent and sharply delineated form in the dispute settlement procedure of the WTO agreement and "third generation" FTAs, has finally refuted the classic "realist" theory concerning the nature and limits of international trade agreements. This realist approach viewed international trade agreements as essentially diplomatic arrangements and assumed that they could never be more than that.<sup>339</sup> Today, the GATT regime is purposefully constructed in such a way as to offer clear rules of conduct regarding trade relations, as well as to achieve decisive, speedy and objective legal determinations in the event of trade disputes between States. In this way, international trade law has apparently reached a level of development which is so far unprecedented in most other fields of public international law,<sup>340</sup> except in regional arrangements, such as the European Union.

From the above analysis, it is apparent that, in recent years, a "world society," a society which is characterized by increasing cross-sector interaction (i.e., between States, corporations and individuals) and by the construction of a legal-organizational regime to regulate this interaction, has begun to coalesce within the arena of international economics. It is a society characterized by the increasing economic interdependence of its members, which possesses a relatively high level of ideological homogeneity, at least in so far as touches the fundamental rules of its common economic regime. Liberal economic perceptions, giving priority to achieving economic prosperity and social security as opposed to building military power and advancing expansionist aspirations, and reliance on peaceful relations together are

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<sup>337</sup> "Agreements must be observed"; this rule is also entrenched in Article 26 of the Vienna Convention on the Law of Treaties, May 23, 1969, 1155 U.N.T.S. 331, 339. Similarly, the rule is entrenched in the internal legal systems of all the GATT Member States, and this fact too strengthens the sense of duty to fulfil the obligations which the State takes upon itself.

<sup>338</sup> See HENKIN, *supra* note 336.

<sup>339</sup> See *supra* note 1 and the accompanying text. See also Robert Hudec, *The GATT Legal System: A Diplomat's Jurisprudence*, 4 J. WORLD TRADE L. 615, 665 (1970).

<sup>340</sup> Daniel K. Tarullo states: "the international trade system looks more like a legal system than do the areas of international law traditionally denominated public." Daniel K. Tarullo, *Logic, Myth and International Economic Order*, 26 HARV. INT'L L.J. 533, 533 (1985).



what provided the appropriate platform for the creation of the legal trade regime. The catalyst was the vital need for stability and certainty in world trade on the basis of clear and enforceable rules. Leaders of the "global village," therefore, recognized their need for law no less than the primitive villagers of ancient times.

The new regime has affected areas previously untouched in public international law, although this interstate regime can still not compare, of course, to domestic legal systems of normal countries. The States still strive to preserve their sovereignty and, in the absence of an autonomous enforcement mechanism (such as an execution office), compliance is still ultimately dependent on the acquiescence of the State itself. The legal regime of the WTO will therefore have to be tested, first and foremost, on the ground and, over the course of time, not only on paper. Much will depend on the ability of the WTO institutions to isolate the dispute settlement procedures from political influence and win the confidence of the international community as independent and objective bodies. But this is still not enough. Leaders of States too must show maturity and respect the rulings, even where they are inconvenient politically. Failure to do so may lead to the collapse of the world trade regime, as has already happened in the past.<sup>341</sup>

The identification and mapping of the elements creating the new regime may help us evaluate the future of the world trade regime and the risk of its collapse. The factors considered above indicate that there is no immediate danger of an impending breakdown. There is no reason to suppose that the level of economic interdependence will lessen, or that the process of globalization of the world economy will halt in the near future. On the other hand, the sudden outbreak of a military conflict or the creation of a new strategic-security threat against one of the economic powers may easily affect the international climate and the spectrum of considerations and preferences. Even an ideological climate is something which may change. Already, voices may be heard, both in the North and in the South, opposing the liberal-capitalist concepts underlying GATT. It is claimed that GATT allows the continued colonial exploitation of developing countries and the promotion of swifter economic development at the price of serious harm to the environment. If the heads of the WTO and State leaders fail to heed these voices and find suitable solutions to the criticisms raised within the framework of the regime, then one may expect

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<sup>341</sup> See PETERSMANN, *supra* note 307 and accompanying text.

threats on the continued success of the new legal regime from this direction as well.

Moreover, if the WTO is intended to fulfil the function of leading the "global village" in the area of international economic relations, then it would be appropriate for this leadership and for the rule-making function which it fulfills to be carried out in accordance with the democratic principles of leadership accepted in modern States. One would then argue for the process of "legislation" to be carried out by representatives elected in a democratic manner, by means of a system which reflects all the interests involved and all those who may be affected by the rules to be established. The current situation, in which the debates on trade rules are conducted under cover of secrecy and far removed from the scrutiny of the public, where non-governmental organizations (voicing important interests not always properly represented in governmental mechanisms) have no right to participate, is creating an estrangement between large sectors of the public and the multilateral regime.<sup>342</sup> This regime is likely to be perceived as the fruit

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<sup>342</sup> Recently, this issue has given rise to intense debate, both on the political and academic level, particularly, in connection with the issue of environmental protection *vis-à-vis* free trade. See, e.g., Patti A. Goldman, *Resolving the Trade and Environment Debate: In Search of a Neutral Forum and Neutral Principles*, 49 WASH. & LEE L. REV. 1279 (1992). The author criticizes the secrecy surrounding the dispute settlement process of GATT, and calls for the establishment of a neutral forum for the settlement of trade disputes with the right of participation and *locus standi* given to representatives of both governments and non-government organizations (NGOs). *Id.* at 1285-87, 1296-98. In her view, the GATT principle of "transparency" should be implemented not only in relation to the trade policy of the Member States, but also in relation to GATT proceedings themselves, so as to "practice what you preach." See also Steve Charnowitz, *Participation of Nongovernmental Organizations in the World Trade Organization*, 17 U. PA. J. INT'L ECON. L. 331 (1996), who also advocates granting NGOs the right to participate in the construction of rules (the "legislation") and in dispute settlement proceedings (the "adjudication") of the World Trade Organization; a right which had existed under the Havana Charter for the establishment of the International Trade Organization. See also Richard Shell, *The Trade Stakeholders Model and Participation by Nonstate Parties in the World Trade Organization*, 17 U. PA. J. INT'L ECON. L. 359 (1996). This author argues that it is actually the "legalization" of the dispute settlement process of the WTO which requires steps to be taken to ensure the public legitimacy of the organization. Accordingly, in his view, all the interests and bodies operating in international trade (and not only governments) should be allowed to participate in the decision-making process. Nevertheless, there are also some who oppose this view, and believe that granting *locus standi* to non-governmental bodies and excessive transparency in the proceedings of the organization can only harm the organization by bringing the international trade disputes to the center of media attention. In their view, this is likely to encourage nationalist sentiments and increase political sensitivity. Similarly, it is feared that only groups possessing sufficient means will be able to exercise the right of *locus standi*, and they will make use of this right to promote their private interests and not the interests of the collective. See Philip M. Nichols, *Extension of Standing in World Trade Organization Disputes to Nongovernment Parties*, 17 U. PA. J. INT'L ECON. L. 295 (1996). This author proposes that instead of extending the right of standing, wider participation should be allowed in the dispute settlement panels, so as to include experts in fields other than international trade, such as experts in environmental protection—in disputes relating to

of the labors of unelected technocrats and capitalist interests, a sort of supra-system which undermines the internal democratic system of the State. This is also true of the adjudication process conducted within the framework of the panels, which some argue are not sufficiently open, do not give sufficient consideration to interests which are not economic in nature and do not give a right of hearing to non-governmental bodies, such as environmental organizations and labor organizations.<sup>343</sup> The greater the influence of international trade agreements and the further the juridicization process advances, the more will the "democratic deficiency" of these regimes be apparent, to the detriment of their legitimacy in the eyes of the public. A similar process occurred in the EC,<sup>344</sup> and the continued existence and development of the EC was only made possible by efforts to resolve these types of problems.<sup>345</sup>

Within the framework of the WTO too it will be necessary to solve the problem of the "democratic deficiency," and to find the right balance between the promotion of economic prosperity, on the one hand, and the interest in protecting the environment and other social concerns, on the other. The first steps in this direction have already been taken.<sup>346</sup> If such a balance is achieved, it will be possible to ex-

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this matter—or representatives of the International Labour Organization—in disputes relating to trade restrictions on products manufactured by child labor. In his view, the authority to do so exists under the new DSU. See *supra* note 84, art. 8(1).

<sup>343</sup> *Id.* and accompanying texts.

<sup>344</sup> See, e.g., J.H.H. Weiler, *The Transformation of Europe*, 100 YALE L. J. 2403, 2466-74 (1991). See also J.H.H. Weiler with U.R. Haltern & F.C. Mayer, *European Democracy and its Critics - Five Uneasy Pieces*, HARVARD JEAN MONNET WORKING PAPER No. 1/95.

<sup>345</sup> Thus, for example, it was decided to strengthen the standing of the European Parliament, which is the only body in the European system which is directly elected by all the citizens of the Community. Indeed, it was only decided to proceed with direct elections to the European Parliament in the 1970s, and they were first conducted in 1979. Similarly, the Single European Act 1985 gave the European Parliament, for the first time, the opportunity to take part in the legislative process (which is primarily controlled by the Council of Ministers and the Commission) by means of the "co-operation" procedure. The Maastricht Treaty of 1992 widened this power by establishing the "joint decision" procedure. See T.C. HARTLEY, *THE FOUNDATIONS OF EUROPEAN COMMUNITY LAW* 32-34 (1988); see generally Paul Marquardt, *Deficit Reduction: Democracy, Technocracy and Constitutionalism in the European Union*, 4 DUKE J. COMP. & INT'L L. 265 (1994).

<sup>346</sup> As a result of public criticism, the World Trade Organization has already introduced certain changes for the purpose of promoting transparency. Thus, for example, the Organization now publishes studies prepared by the Secretariat earlier than it did before, and the Secretariat staff conducts informal consultations with non-governmental organizations. See Benedict Kingsbury, *The Tuna-Dolphin Controversy, the World Trade Organization and the Liberal Project to Reconceptualize International Law*, 5 Y.B. INT'L ENV. L. 1, 14 (1994). Similarly, the new memorandum of understanding permits States to make public their positions in disputes conducted within the framework of the Organization. It should also be noted that the World Trade Organization opened a site on the Internet in 1995, for the purpose of supplying routine and up-to-date

pect not a retreat in the juridicization process but, rather, its continued development. The next stage in this process is likely to be the continued integration of public international trade law into the domestic legal systems of the States and the grant of private rights of action by virtue of this to individuals. In practice, this process has already commenced<sup>347</sup> and, if it continues, has the potential to bring down the "Chinese wall," established by the dualist theory,<sup>348</sup> between public international law and domestic law. It appears, therefore, that international trade relations are likely to continue to serve as the new and exciting target to be conquered by the "rule of law."

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information, according to the Secretary-General of the WTO on the grounds that the WTO must ensure that it is understood properly and that the public have access to it. The address of the site is: <http://www.wto.org> It was also recently decided to publish panel and Appellate Body decisions as soon as they are issued and to make them available to the general public.

<sup>347</sup> See, for example, the obligation under the GATT Agreement on Government Procurement, *supra* note 50, to enable direct legal attacks by potential suppliers against procurement proceedings which are contrary to the agreement. See Reich, *supra* note 50, at 425. See also JOHN H. JACKSON ET AL., IMPLEMENTING THE TOKYO ROUND 207-09 (1984).

<sup>348</sup> See DINSTEIN, *supra* note 7, at 128-30.