



China's Participation in the WTO

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18. AGGRESSIVE LEGALISM: THE EAST ASIAN EXPERIENCE AND LESSONS FOR CHINA

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In her article “Aggressive Legalism: The Rules of the WTO and Japan’s Emerging Trade Strategy”¹, Saadia M. Pekkanen first invented the term “Aggressive Legalism” and defined it as “a conscious strategy where a substantive set of international legal rules can be made to serve as both ‘shield’ and ‘sword’ in trade disputes among sovereign states”.² Pekkanen further explained this strategy as using the substantive rules of the WTO to counter what the Japanese Government deems to be the unreasonable acts, requests and practices of its major trading partners.³

1. Aggressive Legalism: the Japanese Experience

Unlike most other frequent users of the GATT/WTO dispute settlement system, such as the United States and the European Communities, Japan’s aggressive legalism is a rather recent phenomenon. Having lost the Second World War against the Allied Countries, Japan was excluded from the Bretton Woods Conference which designed the post-war world economic order, and was not an original contracting party to the General Agreement on Tariffs and Trade (GATT), which provisionally entered into force in 1948. It was not until 1955 Japan finally acceded to the GATT. For more than thirty years after its accession, Japan managed to avoid formal legal confrontation with other contracting parties in the GATT by trying to settle most complaints against it bilaterally with

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¹ Saadia M. Pekkanen, *Aggressive Legalism: The Rules of the WTO and Japan’s Emerging Trade Strategy*, *The World Economy* 24 (2001): pp. 707-737.

² *Id.* at 708.

³ *Id.* at 708.



the complainants before the panel rulings came out.⁴ According to Pekkanen, by 1986, Japan had been the named defendant in eleven cases before the GATT.⁵ Japan's strategy of settling cases bilaterally outside of the GATT legal framework worked so well, however, that only one of those cases (the *leather* case) ever led to a final panel report.⁶ On the other hand, Japan also tried to refrain from bringing complaints in the WTO and has filed only four GATT complaints until 1988.

Many theories have been developed to explain Japan's reluctance to use the GATT dispute settlement system. Ichiro Araki attributed this to the general nature of the Japanese as "reluctant litigants", which, though having been demystified by John O. Haley to a large extent in the domestic context⁷, still remains true when one turns to Japan's record of using international tribunals in settling disputes with other states.⁸ Another reason could be the legal weakness and loopholes in the GATT machinery in the early years, which made GATT panels an unwise choice for settling trade disputes.⁹ Somewhat related to this, the so-called "Glass House" theory held that, as Japan maintained various trade barriers and restrictive practices to manage international trade in several key sectors, strict interpretations of the GATT might not be in Japan's best interest.¹⁰ Moreover, Japan was denied "full" membership of the GATT club upon accession as fourteen contracting parties have invoked the article of non-application – Article XXXV – against Japan, citing as reason that the up-and-coming Japanese exports would overwhelm traditional sectors such as textiles.¹¹ Thus, Japan's trade diplomacy in the early years was focused on bilateral negotiations to persuade those countries to withdraw their invocation of Article XXXV.¹² Araki dismissed this explanation as unconvincing because, first, even though Japan was no longer subject to Article XXXV by the late 1960s, its reluctance to use the GATT dispute settlement mechanism extended well into the 1970 and

⁴ Id. at 708-709.

⁵ Id. at 709.

⁶ Id. at 709.

⁷ John Owen Haley, *The Myth of the Reluctant Litigant*, *Journal of Japanese Studies*, Vol. 4, No. 2. (Summer, 1978), pp. 359-390.

⁸ Ichiro Araki, *Beyond Aggressive Legalism: Japan and the GATT/WTO Dispute*, in *WTO and East Asia: New Perspectives*, 149-175 (Mitsu Matsushita & Dukgeun Ahn eds., Cameron May, London, 2004), at 150. According to Araki, Japan has never had recourse to the adjudicatory process of international tribunals such as the Permanent Court of International Justice or the International Court of Justice either as a complainant or a respondent until the *Southern Bluefin Tuna* case of 2000.

⁹ Pekkanen, *supra* note 1, at 709.

¹⁰ Pekkanen, *supra* note 1, at 709; Araki, *supra* note 8, at 151; see also Bernard Hoekman & Michel Kosteci, *The Political Economy of the World Trading System*, at 87 (Oxford University Press, 2001).

¹¹ Pekkanen, *supra* note 1, at 709.

¹² Id. at 709.



even early 1980s; second, Japan brought its first case in the GATT — the *Import Restrictions* case against Italy — in 1960, while Italy had indeed invoked Article XXXV earlier against Japan; third, Japan was very reluctant to bring actions against those contracting parties which have not invoked Article XXXV against itself as well.¹³ Another explanation, proffered by Hiroko Yamane, points to the trade surplus of Japan, which puts Japan in an awkward position in aggressively demanding access into foreign markets.¹⁴ This theory, however, fails to explain Japan's reluctance to participate in the GATT cases while suffering from chronic trade deficit until the late 1960s as well as Japan's "aggressive legalism" in the recent decades notwithstanding its persistent trade surplus.¹⁵ Araki pointed out that language barrier also played a role in preventing Japan from effectively accessing the GATT dispute settlement system.¹⁶ Last but not least, Japan, a latecomer to the GATT and largely a Civil Law jurisdiction, was unfamiliar with the legalistic features of the GATT dispute settlement system, which, for a long time, was shaped by the United States, which is also the archetype of the Common Law system.¹⁷

Major changes came in the late 1980s, when Japan won two cases at the GATT.¹⁸ One case was the *Spruce-Pine-Fir (SPF) Dimension Lumber* case brought by Canada.¹⁹ In this case, Canada alleged that the Canadian exports of SPF lumber and the American exports of non-SPF lumber are "like products". Thus, Japan violated the Most-Favored Nation clause in GATT Article I by imposing an eight per cent tariff on the former while letting the latter enter the Japanese market duty-free. The Panel ruled that, as tariff differentiation is a legitimate means of trade policy, the burden is on the party challenging such tariff-classification to prove that such differentiation is discriminatory. Canada lost because it failed to provide sufficient evidence. Pekkanen argues that this case marked the shift of Japan's trade strategy to "aggressive legalism" as it drastically affected the domestic Japanese perception of the GATT at two levels: one is that the GATT is fair towards all of its members; the other is that the GATT is useful as a legal weapon against foreign complaints and pressures.²⁰ Araki, however, doubts the significance of this case as the watershed of Japan's shift to "aggressive legalism" as this was only a

¹³ Araki, *supra* note 8, at 151.

¹⁴ Hiroko Yamane, *The WTO Dispute Settlement Mechanism and Japanese Traders*, *Journal of International Economic Law* 1998, 1(4), 683-689, at 689.

¹⁵ Araki, *supra* note 8, at 151.

¹⁶ Araki, *supra* note 8, at 151.

¹⁷ For the influence of the United States on the legalization of the GATT, see e.g., Michael J. Trebilcock & Robert Howse, *The Regulation of International Trade* (New York: Routledge, 1999, 2nd ed.), pp. 52-53.

¹⁸ Pekkanen, *supra* note 1, at 709-710; 3-4.

¹⁹ *Canada/Japan: Tariff on Imports of Spruce, Pine, Fir (SPF) Dimension Lumber*, Report of the Panel adopted on 19 July 1989 (L/6470 – BISD 36S/167).

²⁰ Pekkanen, *supra* note 1, at 710.



defensive case for Japan.²¹ Araki argues that the real turning point should be a case in which Japan started using the GATT dispute settlement mechanism actively to counter the “unfair” trade practice of its trade partners.²² According to Araki and Yuji Iwasawa, the truly historical case is the *Parts and Components* case²³ brought by Japan against the European Communities.²⁴ The case was preceded by a string of unfavorable rulings against Japan in the GATT, which made it all the more urgent for Japan to “assert its rights when it had a good case”.²⁵ In that case, to counter the “screwdriver” operations that circumvent anti-dumping duties on finished products, the European Communities passed a law which would impose definite anti-dumping duties against even final products that are assembled or produced in the Community, if such assembly or production is conducted by a party which is related or associated to a manufacturer whose exports of such like final products are subject to definite anti-dumping duties. Japan challenged this law as violating, *inter alia*, the National Treatment clause in GATT Article III. The Panel sided with Japan and ruled against the European Communities.

Notwithstanding their disagreement as to exactly which case started Japan off down the road on aggressive legalism, Pekkanen, Araki and Iwasawa all observe that, for good or bad, Japan's aggressive legalism is here to stay.²⁶ Such strategy takes different forms on different levels. At the domestic level, since 1992, Japan has been publishing the Hukosei Boeki Hokokusho (“Unfair Trade Report”), which, available in both Japanese and English, purports to document the WTO-inconsistent trade practices of its major trade partners.²⁷ At the multilateral level, in order to contain the aggressive unilateralism of the United States, Japan teamed up with contracting parties such as the European Communities and India to further strengthen the dispute settlement rules during the Uruguay Round negotiations.²⁸ Currently, Japan is also an active participant of the ongoing Dispute Settlement Understanding (DSU) review negotiations. In terms of the actual use of the multilateral dispute

²¹ Araki, *supra* note 8, at 152.

²² Araki, *supra* note 8, at 152.

²³ *EEC – Regulation on Imports of Parts and Components*, Report by the Panel adopted on 16 May 1990(L/6657 – BISD 37S/132).

²⁴ See Yuji Iwasawa, *WTO Dispute Settlement and Japan*, in *New Directions in International Economic Law – Essays in Honour of John H. Jackson*, at 477 (Marco Bronckers & Reinhard Quick, eds., Kluwer Law International, 2000). See also Araki, *supra* note 8, at 152-153.

²⁵ Araki, *supra* note 8, at 153.

²⁶ Pekkanen, *supra* note 1, at 732; Iwasawa, *supra* note 24, at 477; Araki, *supra* note 8, at 170.

²⁷ Pekkanen, *supra* note 1, at 711; Araki, *supra* note 8, at 154.

²⁸ Araki, *supra* note 8, at 154.



settlement system, Pekkanen argues that Japan's aggressive legalism include both "Shield" and "Sword" aspects: first, the Japanese Government uses the legal rules as a "Shield" which provides a cover for domestic measures and institutions no matter how controversial they may appear to Japan's trade partners; second, the Japanese government uses the legal rules as a "Sword" which allows it to challenge foreign measures that it deems to be controversial.²⁹ The first group includes cases such as the *Kodak-Fuji* dispute, while the second group includes cases such as the *Section 301 (Automobiles)* case. Japan's aggressive legalism became even more firmly established after the establishment of the WTO. Up until 2004, Japan has brought 12 complaints in the WTO, and has also defended itself in 14 cases brought by other members. The important point, as made clear by Pekkanen, is not "simply about winning or losing"; rather, the point is that "Japan is no longer hesitant about using the WTO legal rules and processes to challenge its trade partners in a visibly confrontational manner irrespective of the legal outcomes".³⁰

2. Aggressive Legalism: the Korean Experience

With Japan setting the trend, other East Asian countries seem to be quick to follow. One notable example is Korea. Even though it started to join the GATT as early as in 1950, Korea did not become a contracting party to the GATT until 1967 due to the disruption of the Korean War.³¹ Since then, Korea's participation in the GATT dispute settlement system has been rather meager. Until the establishment of the WTO in 1995, Korea has been sued in only two cases, namely the *Korea – Beef I* case and the *Korea – Polyacetal Resins* case; while Korea has brought only one complaint, the *EC – Korean Television Sets* case (which was later settled).³² Overall, Korea was leaning towards the more pragmatic approach and tried to avoid formal dispute settlement as much as possible.³³ Korea's reluctance to use the GATT dispute settlement system is, by no means, however, a reliable indication of its experience with foreign trade barriers.³⁴ On the contrary, Korea was a frequent target of the restrictive trade practices of contracting parties such as the United States, the European Communities, Canada and Australia.³⁵ From 1960 to 1994, Korea was subject to about 300 trade remedy measures. Also, among

²⁹ Pekkanen, *supra* note 1, at 713.

³⁰ *Id.* at 732.

³¹ Dukgeun Ahn, *Korea on the GATT/WTO Dispute Settlement. System: Legal Battles for Economic Development*, 6 *Journal of International Economic Law* (2003), at 598-601.

³² *Id.* at 601-602.

³³ *Id.* at 607.

³⁴ *Id.*

³⁵ *Id.*



the 98 Section 302 cases initiated between 1975 and 1994, Korea has been targeted 10 times.³⁶ Trying to explain the paradox, Ahn provides three reasons: first, the Korean Government lacked sufficiently competent staffs to handle the legal technicalities of the GATT legal system; second, traditionally, Korean culture regarded legal confrontation as the demise of normal diplomatic relationships with concerned states; third, Korea generally maintained high trade surplus against those countries that routinely imposed trade remedy measures, and such trade surplus usually undermined the political willingness of the Korean Government in asserting its rights under the GATT in a legalistic manner.³⁷

After the establishment of the WTO, Korea became more and more active in using the dispute settlement system to assert its legal rights.³⁸ In the first five cases brought by other Members against Korea, however, the Korean Government has taken a cautious approach and tried to settle them by consultations.³⁹ As explanations, Ahn points to the fact that the merits in these cases were relatively clear, and the economic stakes were not substantial.⁴⁰ Also, Korea was still not ready to deal either with the procedural issues of the new WTO dispute settlement system or the novel substantive issues raised by these cases concerning the Sanitary and Phytosanitary Agreement and the Agreement on Technical Barriers to Trade.⁴¹

The case of *Korea – Taxes on Alcoholic Beverages*⁴² marked a shift of Korea's trade strategy to aggressive legalism. In that case, the European Communities and the United States challenged the Korean liquor taxes system, which, at 100 per cent on whisky and 35 per cent on diluted *soju*, violated the National Treatment obligation under GATT Article III.⁴³ Before both the Panel and the Appellate Body, Korea tried to argue that, because the two products are not competing against each other, they are not "like products" as defined under Article III.⁴⁴ The Panel and the Appellate Body disagreed and Korea eventually lost this case. The importance of the case does not lie so much in the fact that it was the first full WTO case involving Korea, but rests on the importance of *soju*,

³⁶ Id. at 608.

³⁷ Id. at 608-609.

³⁸ Id. at 609.

³⁹ Id. at 610-611.

⁴⁰ Id. at 611.

⁴¹ Id.

⁴² Appellate Body Report, *Korea – Taxes on Alcoholic Beverages*, WT/DS75/AB/R, WT/DS84/AB/R, adopted 17 February 1999, DSR 1999:I, 3.

⁴³ Ahn, *supra* note 31, at 611-612.

⁴⁴ See e.g. paras. 4-15 of the AB report.



the product concerned, at a level incomparable by any other products in Korea.⁴⁵ With all the media attention on this case, the Korean Government can no longer try to settle this case by making secret deals with its trade partners, just like it did in the prior cases.⁴⁶ Instead, in order to show that Korea will not budge under foreign pressures, the Korean Government was forced to play the intricate legal game of the WTO dispute settlement system, albeit with the assistance of foreign lawyers.⁴⁷ After the WTO ruling came out, the Korean government complied by raising the tax rate for *soju*, rather than reducing the tax rate for whisky to that of *soju*, in order to eliminate the WTO-illegal tax gap while minimizing the potential adverse impact on public health and consequent social costs.⁴⁸ As a result, even the general public can feel the impact of the WTO dispute settlement system at the deepest and widest level of everyday life.⁴⁹ Thus, from the point of enhancing the public awareness of the WTO dispute settlement system, Korea probably has benefited more by losing rather than winning this case.

With the lessons learned in the hard way, Korea is now set to embark on the road to aggressive legalism. In all the following cases brought against Korea, Korea has stood firm to play the legal game.⁵⁰ Moreover, Korea also started actively using the WTO dispute settlement system to challenge the trade measures of other Members. From 1997, Korea has brought seven cases in the WTO. These cases all concern trade remedies. In terms of countries concerned, they are almost all, with the exception of one, directed against the United States.⁵¹ This is rather strange as among the relevant period, it was the European Communities that brought most anti-dumping investigations against Korea, while South Africa and India actually imposed the most anti-dumping measures against Korea.⁵² The only feasible explanation, as offered by Ahn, seems to be that the Korean exports rely heavily on the United States market.⁵³ Also, Korea has participated in many cases as a third party.⁵⁴ Presumably, such participation is helpful for Korea to present its views and protect its economic interests, but it also provides Korea with an opportunity to hone its legal skills and become more familiar with the WTO dispute settlement system.⁵⁵

⁴⁵ Ahn, *supra* note 31, at 612.

⁴⁶ *Id.*

⁴⁷ *Id.*

⁴⁸ *Id.*

⁴⁹ *Id.* at 612-613.

⁵⁰ See, *id.* at 613-617.

⁵¹ *Id.* at 617-626.

⁵² *Id.* at 625.

⁵³ *Id.*

⁵⁴ *Id.* at 626.

⁵⁵ *Id.*



Summarizing the experiences of Japan and Korea as above, we can discern a clear trend of both countries making the shift from pragmatism towards “aggressive legalism”, or, in other words, from reluctant litigants to active users of the GATT/WTO dispute settlement system. As Pekkanen has observed, “the core idea behind aggressive legalism is the active use of the legal rules in the treaties and agreements overseen by the WTO to stake out positions, to advance and rebut claims, and to embroil all concerned in an intricate legal game. . . . [i]t is meant to be measured, slow, and cautious, *carefully trapping everything into the legitimate game of legal tactics*”.⁵⁶ Pekkanen further identifies four major advantages of such strategy to the Japanese Government.⁵⁷ To sum up, however, the biggest benefit of aggressive legalism is that it provides Japan with a legitimate means both to shield trade policies that it deems legitimate no matter what are the reactions of its trade partners, and to say no to pressures and requests from its trade partners that it deems unreasonable; it provides Japan with an open and transparent means to deal with its trade partners, so that it could conduct its foreign trade with marked independence.⁵⁸ Such a strategy is useful for Japan, a country that, for historical reasons, relies heavily on the United States both politically and economically. Such a strategy is useful for most other countries as well because almost all major trading nations in the world inevitably have to deal with the *aggressive unilateralism* of the United States and *aggressive legalism* seems to be the only workable response. In this regard, one can not help but agree with Pekkanen in observing that: “[i]t is not important whether Japanese officials fundamentally believe in the procedural and substantive fairness of the legal rules of the WTO. Rather, the important point is that they are willing to use them to buttress their positions and arguments in confronting their trade partners.”⁵⁹

3. Aggressive Legalism: Time for China?

With such obvious benefits, it seems only logical that China, the next East Asian trade power, would quickly jump on the aggressive legalism bandwagon. Both Pekkanen and Araki predicted that this would be the case⁶⁰, while Youngjin Jung seemed to confirm this prediction with his article.⁶¹ After discussing the first provisional safeguard measure imposed by the Chinese Government in response to the steel trade war

⁵⁶ Pekkanen, *supra* note 1, at 732 (emphasis added).

⁵⁷ *Id.* at 733.

⁵⁸ *Id.*

⁵⁹ *Id.*

⁶⁰ Pekkanen, *supra* note 1, at 735; Araki, *supra* note 8, at 171.

⁶¹ Youngjin Jung, *Aggressive Legalism: China's First Safeguard Measure*, *Journal of World Trade* 36(6): 1037–1060, 2002.



set off by the United States, Jung rushed to conclude that China has shown a “penchant” for aggressive legalism.⁶² Closer examinations seem to indicate, however, that this observation is rather premature. For one thing, Jung does not seem to fully appreciate the special meaning of the term “aggressive legalism”, which refers to the use of WTO *dispute settlement system* in order to solve *trade disputes* at the *multilateral* level. The application of safeguard measures, however, is something that is entirely different. First, such measures are not directed at disputes. The WTO agreements do not have a direct definition of what constitutes a “dispute”. Article 3.3 of the DSU, however, provides an indirect definition by noting that disputes are “situations in which a Member considers that any benefits accruing to it directly or indirectly under the covered agreements are being impaired by measures taken by another Member”. A key element in this definition is that there must be “measures taken by another Member”. Safeguard measures, however, do not seek to address government measures taken by another Member. The Agreement on Safeguards states in Article 2.1 that safeguard measures are to be applied on a product only if “such product is being imported into its territory in such increased quantities, absolute or relative to domestic production, and under such conditions as to cause or threaten to cause serious injury to the domestic industry that produces like or directly competitive products”. This in no way refers to any conscientious actions taken by foreign governments. In practice, all safeguard measures are taken as a response to the increase in imports due to decisions by private firms. Thus, safeguard measures are not taken against trade disputes, even though such measures themselves, in so far as they are measures taken by governments, might become subjects of trade disputes. Second, such measures are not taken at the *multilateral* level. Instead, they are the actions taken by individual Members *unilaterally* according to its own domestic law. The recent safeguard investigations by both the EC and US against Chinese textile products show that such measures can be concerted actions of several WTO Members at the same time, but this does not change the unilateral nature of safeguard measures. In this regard, Jung might have mixed up the concepts of “aggressive legalism” with “aggressive unilateralism” (or in China’s instance, as the Chinese measures are not so at odds with WTO rules, with “not-so-aggressive unilateralism”). Third, such measures do not involve the WTO dispute settlement system. They are investigations conducted by the administrative agencies in China, and as such does not involve dispute settlement at all, not to mention the WTO dispute settlement system.

⁶² Id. at 1060.



In his article, Jung also mentioned the case brought by China against the US safeguard measures at the WTO.⁶³ As discussed in the paragraph above, this is where the analysis on China's "aggressive legalism", if there is any, should start. Unfortunately, Jung took the wrong route by wholly ignoring this case and focusing instead on provisional safeguard measure in order to examine "the force of China's aggressive legalism"⁶⁴.

One reason for Jung's reluctance was probably due to the fact that by the time his article was published, the *US-Steel Safeguard* case has yet been decided.⁶⁵ With the Appellate Body report in that case adopted on December 10, 2003, it might be time now to reflect on the case.

3.1 US-Steel Safeguard⁶⁶

This case concerns the safeguard measures imposed by the United States on several steel products. In June 2001, pursuant to the request from the United States Trade Representative's Office (USTR), the US International Trade Commission (ITC) initiated a safeguard investigation on certain steel products. On the basis of the report of the ITC, the US President issued in 5 March 2002 Proclamation No. 7529 and imposed 11 distinct safeguard measures applicable to 15 steel products. The measures affected the steel exports of many WTO Members and provoked major reactions from around the world. The EC quickly requested consultations with the US, and several other countries, including China, also followed suit. On 7 May 2002, the EC requested the establishment of panel. China also made the request on 27 May 2002. Brazil, Japan, Korea, New Zealand, Norway and Switzerland also joined in the complaint. In its report circulated on 11 July 2003, the Panel declared all safeguard measures inconsistent with the WTO rules as the US authorities fail to provide "reasoned and adequate" explanations to its decisions. This ruling was later affirmed by the Appellate Body in its report circulated on 10 November 2003.

While some commentators might hail this case as the start of China's aggressive legalism, the author would be more hesitant in making such a claim. The central element of aggressive legalism is the process rather

⁶³ Id. at 1038, 1042.

⁶⁴ Id. at 1039.

⁶⁵ The article was published in December 2002, while the Appellate Body report in that case was issued in December 2003.

⁶⁶ Appellate Body Report, *United States – Definitive Safeguard Measures on Imports of Certain Steel Products* ("US – Steel Safeguards"), WT/DS248/AB/R, WT/DS249/AB/R, WT/DS251/AB/R, WT/DS252/AB/R, WT/DS253/AB/R, WT/DS254/AB/R, WT/DS258/AB/R, WT/DS259/AB/R, adopted 10 December 2003.



than the results. For a WTO Member which adopts the strategy of aggressive legalism, the most important thing is not to win a case; rather, it is to use the WTO dispute settlement system to attack others or defend itself based on WTO rules. As put by Pekkanen, “the core idea behind aggressive legalism is the active use of the legal rules in the treaties and agreements overseen by the WTO to stake out positions, to advance and rebut claims, and to *embroil all concerned in an intricate legal game*.....[i]t is meant to be measured, slow, and cautious, *carefully trapping everything into the legitimate game of legal tactics*”.⁶⁷ It is hard to say, however, that China’s decision to join the Steel Safeguard case was driven by these concerns. Instead, China’s decision to file a complaint was influenced by the following factors.

First, there was a strong team of co-complainants. Of the eight Members that filed the complaint, EC, Japan, Korea and Brazil are among the most active users of the WTO dispute settlement system. Thus, even though China also joined the case as a complainant, the case was not simply, as some Chinese media would put it, China against the US. The more accurate picture is the EC, or EC-Japan-Korea-Brazil against the US, with China hiding in the shadow of the EC. This can be clearly discerned from the sequence of events, where China co-ordinated its positions with the major complaints such as the EC, Japan and Korea, and waited until the EC, Japan and Korea has filed their complaints to file its own. To borrow an old Chinese saying, what China was doing in this case is just “beating the drowning dog”, while China was not the one that had the audacity to push the dog into the river in the first place. Of course, China is not the only one that joins the dog-beating squad: Switzerland and Norway, two countries that has never participated in any panel as complainants before, also quickly jumped on the bandwagon. This further confirms the theory that China is only piggy-backing on the EC, Japan, Korea and Brazil.

Second, there was bad publicity against the US from the very beginning. Within days of the announcement of the safeguard measures, major media from around the world joined the chorus of condemning the US.⁶⁸ As one commentator put it, “the US has lost the case even before it went

⁶⁷ Pekkanen, *supra* note 1, at 732 (emphasis added).

⁶⁸ See e.g., Raymond Colitt, et al., *World United to Condemn US Decision to Impose 30% Tariffs*, Financial Times, Mar 7, 2002, at 8; David Teather, et al., *US puts steel into trade war with EU: Bush imposes 30% tariffs on imports*, The Guardian (London), March 6, 2002, at 25; Paul Blustein, *EU Challenges US Steel Tariffs at WTO*, The Washington Post, March 8, 2002, at E03; Ben Russell, et al, *Trade War: Blair Joins Global Attack On ‘Unjustified’ Tariffs; European and Asian Leaders Prepare to Impose Tit-For-Tat Sanctions after American Move to Protect Steel Industry*, The Independent (London), March 7, 2002, at 15; Editorial: *US move sends wrong signals*; The Daily Yomiuri (Tokyo), March 7, 2002, at 16.



to Geneva". Article 11 of the DSU requires the panelists to "make an objective assessment of the matter before it". To ensure the objectivity of panel decisions, Article VI of the Rules of Conduct for the Understanding on Rules and Procedures Governing the Settlement of Disputes ("Rules of Conduct") requires Panelists and Appellate Body Members to disclose "any information that could reasonably be expected to be known to them at the time which, coming within the scope of the Governing Principle of these Rules, is likely to affect or give rise to justifiable doubts as to their independence or impartiality". Annex 2 to the Rules of Conduct provides an illustrative list of such information, and this include under item (d) "considered statements of personal opinion on issues relevant to the dispute in question (eg publications, public statements)". This seem to include only statements made by such person himself, rather than the statements made by someone else, even if the statement of the latter might have a heavy influence on the former. This is confirmed by Article 13 of the DSU, which gives the panel broad discretion in seeking "information and technical advice from any individual or body". In the US, to prevent the jury from being swayed by biased news reports, the judge would lock the jury up for the period of the trial. At the WTO, however, this is impossible as the panelists and even Appellate Body members are serving on a part-time basis only. They usually have full-time jobs somewhere else, and would only be in Geneva for a dozen days during the course of the panel/Appellate Body process. They are not prohibited from reading news reports that side with one position or another. As a matter of fact, most of them do indeed read such news reports with great interests. One might argue that, as panelists should be "well-qualified governmental and/or non-governmental individuals"⁶⁹, it is unlikely that they will be influenced by journalism. In reality, however, things are not quite as it should be. In several cases, panelists who are not so "well-qualified" have been appointed. Even in cases where the panelists are indeed up to the standard, it is not uncommon to see panelists who do not bother to read all the submissions at all because they are serving on a part-time basis.⁷⁰

Third, every safeguard measure that has been challenged at the WTO has been declared illegal. Before the *US – Steel Safeguard* case, there have

⁶⁹ Article 8 of DSU.

⁷⁰ Panelists usually are in Geneva only for the days of the oral hearing and internal deliberation, which would normally come to only a dozen days for a case. To make the matter even worse, they can only claim fees for a limited number of days for the time they spend in preparing for the meetings in Geneva no matter what the actual preparation time might be. This has provided further disincentive for the panelists to devote their time to study the written submissions made by the parties.



been seven safeguard cases before the WTO panel and Appellate Body.⁷¹ In all cases, the panel and/or Appellate Body has found the safeguard measure at issue violated the Safeguard Agreement and Article XIX of the GATT 1994.⁷² The Appellate Body articulated its strong distaste of safeguard measures by stating in *Argentina – Footwear*: “[T]he import restrictions that are imposed on products of exporting Members when a safeguard action is taken must be seen, as we have said, as extraordinary. And, when construing the prerequisites for taking such actions, their extraordinary nature must be taken into account.”⁷³ The classical justification for safeguard measure is that countries are more likely to undertake broader trade liberalizations if they know that they could suspend them should they encounter difficulties in implementing such obligations.⁷⁴ This makes sense in theory. In reality, however, safeguard measures are mostly invoked at the pressures of protectionist groups. When a sector is flooded with increased foreign imports, it usually has also been hit with many other problems of its own making. Indeed, if they weren’t having these home-grown problems, the foreign products would not have flooded the market in the first place.⁷⁵ Infested with problems such as rising costs of materials, obsolete equipment, pension costs to retired workers, the US steel industry is among the least efficient in the world. Therefore, it is no surprise that the US steel safeguard has been looked upon with suspicious eyes. Even the US Government conceded this, albeit reluctantly, in the 11 March 2003

⁷¹ They are: *Argentina–Footwear Safeguards*, *Argentina–Peach Safeguards*, *Chile–Agricultural Products (Price Band)*, *Korea–Dairy Safeguards*, *US–Lamb Safeguards*, *US – Line Pipe Safeguards*, *US–Wheat Gluten Safeguards*.

⁷² Alan Sykes points out that, the requirement of “unforeseen developments” under Article XIX has been largely ignored by the contracting parties during the GATT era, and the WTO Agreement on Safeguards also omits any reference to ‘unforeseen developments’ or the ‘effect of the obligations incurred’. The Appellate Body, however, has brought the “unforeseen developments” requirement back by reading Article XIX and the Safeguards Agreement cumulatively. To make it even worse, the Appellate Body also fails to articulate any coherent doctrine as to when safeguard measures are allowable. He suggests that this is the reason why safeguard measures have never been upheld in the WTO. See Alan Sykes, *The Safeguards Mess: A Critique of WTO Jurisprudence*, *WORLD TRADE REVIEW* (2003), 2: 3, 261–295.

⁷³ Appellate Body Report, *Argentina – Safeguard Measures on Imports of Footwear*, WT/DS121/AB/R, adopted 12 January 2000, DSR 2000:I, 515, at para 94. This has been quoted over and over again in several other cases, including *inter alia*, Report of the Panel, *United States – Safeguard Measures on Imports of Fresh, Chilled or Frozen Lamb Meat from New Zealand and Australia*, 21 December 2000, at para 7.18; Report of the Appellate Body, *United States – Safeguard Measures on Imports of Fresh, Chilled or Frozen Lamb Meat from New Zealand and Australia*, 1 May 2000, at para 124; and Report of the Appellate Body, *United States – Definitive Safeguard Measures on Imports of Circular Welded Carbon Quality Line Pipe from Korea*, 15 February 2002, at para.81.

⁷⁴ See Sykes, *supra* note 71, at 262, 288–291; see also Trebilcock & Howse, *supra* note 17, at 230.

⁷⁵ Alan Sykes also offers a succinct critique of the “efficiency” rationale of safeguard measures. See Sykes, *supra* note 71, at 261–286, 287.



letter by the then Deputy USTR Linnet Deily to then WTO Director General Mike Moore, which acknowledged that “the US steel industry is not immune from the need for reform” but “must continue to restructure and retool as well”.⁷⁶

Last but not least, the most bizarre feature of this case is that even the respondent itself was urging the complainants to bring the case to the WTO dispute settlement system. In her aforementioned letter to Mike Moore, Ambassador Deily was literally begging the other WTO Members to file a WTO complaint by noting, in three different paragraphs, that “[t]o the extent [a WTO Member] considers that the USITC’s findings ...incorrect”, it must “bring its complaint... before the World Trade Organization to be resolved under multilaterally-agreed dispute settlement procedures”, which is “the right place to resolve differences”.⁷⁷ Why was the US so eager to be dragged to court? To answer this question, we have to answer another question: what was the US afraid of, or, what is the other option(s) available to other WTO Member? Apparently, the US was afraid of retaliation from the EU. Both Article XIX.3 of the GATT 1994 and Article 8 of the Agreement on Safeguards give the right of the affected exporting Members to seek compensation or suspend concessions to the Member applying the safeguard measure. Legally speaking, the compensation requirement is needed in order to maintain the balance of rights and obligations among WTO Members.⁷⁸ In economic terms, the compensation requirement does not seem to make sense. If the safeguard user is having genuine difficulties in complying with its WTO obligations, the suspension of concessions by other Members will only exacerbate the problem. Putting in the perspective of real-world politics, however, this makes perfect sense. Safeguard measures and the retaliation usually target different sectors/industries, and it is an open secret that politicians make their living by catering to the interests of strong political lobbies at the cost of other weaker or less well-organized interest groups. The US might well be sitting on their hands and watch the Europeans retaliate by raising the tariffs of some widgets which nobody cares about. Unfortunately, in this particular case, the US faced someone which knows them too well. The EU, by issuing Council Regulation No 1031/2002 on 13 June 2002, announced that it would *suspend* its tariff concessions granted to the US from 18 June 2002, and apply *additional duties* of up to 100 per cent on

⁷⁶ The United States Mission to the European Union, *USTR’s Deily Defends Steel Tariffs Decision, Rebuts EU Demands* (visited August 3, 2005) <<http://www.useu.be/Categories/Trade/Steel/Mar1102USTRDeilySteel.html>>.

⁷⁷ *Id.*

⁷⁸ Art. 8, Agreement on Safeguards.



such products from as early as August 1, 2002.⁷⁹ The retaliation list includes products from many politically sensitive states, such as citrus fruits (Florida), textiles (Carolinas), Harley-Davidson motorcycles (Wisconsin). In the grand scheme of things, the steel safeguard was part of the horse-trading efforts by President Bush in order to garner congressional support for the Trade Promotion Authority (TPA), which would allow comprehensive trade deals sent to Congress for approval by the President to receive up or down action by the Senate and the House of Representatives without amendment. The EU retaliation, however, might well cost him the next presidential election by undermining the support from these crucial states. Moreover, under GATT Article XIX:3(a) and Article 8.3 of the Agreement on Safeguards, the EU has a right to impose unilateral retaliations not later than ninety days after the application of the safeguard measure. This is different from the normal procedure of seeking implementation of panel/Appellate Body rulings or compensation, under which the respondent usually can delay the process for three years or more by exploiting the loopholes in the WTO dispute settlement procedures. Thus, it is no wonder that the US was urging the complainants to take the case to the WTO. Indeed, the US seemed to be playing the delay tactic again in this case as the President terminated the steel safeguards immediately following the Appellate Body decision.⁸⁰

To sum up, China's decision to join as a co-complaint was more of the result of a combination of all the unique features in this case, rather than driven by its desire to embrace aggressive legalism. Moreover, even though the case was hailed as "China's first victory in the WTO" and widely reported in the Chinese media, it did not persuade the Chinese Government to embark on the road of aggressive legalism and lodge more complaints after that.⁸¹ On the contrary, China has been trying to avoid resorting to the dispute settlement mechanism as much as it could, as are evidenced by another two brief encounters it had with the mechanism.

3.2 China – Value Added Tax on Integrated Circuits

On 18 March 2004, the US made a request for consultations to China regarding China's value-added tax ("VAT") on integrated circuits

⁷⁹ Articles 1, 2, 3 and 4 of the Council Regulation No 1031/2002 (emphasis added).

⁸⁰ Joost Pauwelyn, *WTO Victory on Steel Hides Deficiencies* (visited August 3, 2005) <<http://jurist.law.pitt.edu/forum/Pauwelyn1.php>>.

⁸¹ Jiang Liyong, *WTO Dispute Settlement Mechanism and China's Participation*, in *CHINA'S PARTICIPATION IN THE WTO*, (Henry Gao & Don Lewis eds., Cameron May, London, 2005).

⁸² *China - Value-Added Tax on Integrated Circuits*, Request for Consultations by the United States, WT/DS309/1.



("ICs").⁸² According to Art. 4.4 of the DSU, such request "shall give the reasons for the request, including identification of the measures at issue and an indication of the legal basis for the complaint". The United States provided its reasons as follows:

"China provides for a 17 per cent VAT on ICs. However, we understand that enterprises in China are entitled to a partial refund of the VAT on ICs that they have produced, resulting in a lower VAT rate on their products. China therefore appears to be subjecting imported ICs to higher taxes than applied to domestic ICs and to be according less favorable treatment to imported ICs.

In addition, we understand that China allows for a partial refund of VAT for domestically-designed ICs that, because of technological limitations, are manufactured outside of China. China thus appears to be providing for more favourable treatment of imports from one Member than another, and discriminating against services and service suppliers of other Members."⁸³

As to the measures at issue, the US cited six regulations various Chinese ministries issued from June 2000 to December 2003.⁸⁴ The first and most important one is the Notice of the State Council Regarding Issuance of Certain Policies to Promote the Development of the Software Industry and Integrated Circuit Industry of 24 June 2000, which is popularly known as the Document 18 because its file number is 2000-18. As its title suggests, Document 18 aims at promoting the development of China's software and IC industries. In its 53 articles grouped in 13 chapters, Document 18 lists several preferential policies on investment, tax, technology development, export, income distribution, human

⁸³ *China – Value-Added Tax on Integrated Circuits*, Request for Consultations by the United States, WT/DS309/1.

⁸⁴ They are: Document 18 (24 June 2000), Notice of the State Council Regarding Issuance of Certain Policies Concerning the Development of the Software Industry and Integrated Circuit Industry; Document 25 (22 September 2000), Notice of the Ministry of Finance, State Administration of Taxation, and General Administration of Customs on Relevant Tax Policy Issues Concerning Encouraging the Development of the Software Industry and the Integrated Circuit Industry; Document 86 (7 March 2002), Notice of the Ministry of Information Industry Regarding Issuance of Regulations on Certification of Integrated Circuit Design Enterprises and Products; Document 70 (10 October 2002), Notice of the Ministry of Finance, State Administration of Taxation Regarding Furthering Tax Policies to Encourage the Development of the Software Industry and Integrated Circuit Industry; Document 140 (25 October 2002), Notice of the Ministry of Finance, State Administration of Taxation Regarding Tax Policies for Imports of Integrated Circuit Products Domestically Designed and Fabricated Abroad; and Document 1384 (23 December 2003), Notice of the State Administration of Taxation Regarding Issuance of the Catalogue of Integrated Circuit Products Enjoying Preferential Tax (First Batch).



resource, government procurement and protection of intellectual property rights. The complaint of the United States concerns two articles. One is Article 41, which provides a rebate of the amount of the effective value-added tax (VAT) burden in excess of 6 per cent for ICs manufactured within China, while the statutory VAT rate of 17 per cent on sales of all imported and domestically-produced ICs is 17 per cent. On 10 October 2002, the Ministry of Finance and State Administration of Taxation issued another notice to further expand the VAT rebate to any tax burden that exceeds 3 per cent. The other is Article 48, which, together with the Notice of the Ministry of Finance, State Administration of Taxation Regarding Tax Policies for Imports of Integrated Circuit Products Domestically Designed and Fabricated Abroad, provides tax rebate of the amount of the effective VAT burden in excess of 6 per cent for ICs designed in China but fabricated abroad due to the lack of technological capacities domestically.

For the legal basis, the US cites Articles I and III of the GATT 1994, the Protocol on the Accession of the People's Republic of China (WT/L/432), and Article XVII of the GATS.

As explained by the Appellate Body in *EC — Bananas III*, the DSU does not require the complainant to list the detailed arguments in its request.⁸⁵ Thus, the US did not state specifically how the measures at issue violate the relevant legal provisions. In the view of the author, the US might make the following arguments:

- A. Article 41 rebate makes the VAT rate for domestically manufactured ICs lower than that for imported ICs, thus violates the national treatment obligation under GATT Article III;
- B. For imported products, Article 48 rebate makes the VAT rate for those designed in China lower than that for those designed abroad, thus violated the most-favored-nation (MFN) obligation under GATT Article I;
- C. For IC design services and service providers, Article 48 rebate makes the VAT rate for those services and service providers in China lower than that for those services and service providers abroad, thus violated the national treatment obligation under GATS Article XVII.

⁸⁵ Appellate Body Report, *European Communities — Regime for the Importation, Sale and Distribution of Bananas*, WT/DS27/AB/R, adopted 25 September 1997, DSR 1997:II, 591, at para 141.

In response, China might make the following counter-arguments:

- A. The rebates are subsidies provided to the *producers*, which would fall under the exception for “subsidies exclusively to domestic producers” under Article III.8(b). They are not subject to Article III, which only prohibits discrimination between domestic and imported *products*.⁸⁶ This argument, however, is unlikely to succeed. As clarified by the Appellate Body in *Canada – Periodical*, Article III:8(b) was intended to exempt from the obligations of Article III “only the payment of subsidies which involves the expenditure of revenue by a government” and could not be construed to “sanction the exemption of domestic products from internal taxes imposed on like imported products or the remission of such taxes”.⁸⁷
- B. The statutory tax rate is different from the effective rate. In practice, the effective tax rate of the imported products and domestic products are almost the same. Thus, there is no *de facto* discrimination.⁸⁸ However, it has long been settled that the WTO obligations applies to both *de jure* and *de facto* discriminations.⁸⁹

The US also referred to China's Accession Protocol in its request. Again it did not mention the specific provisions, but there are two parts that might be relevant in this case. One is paragraph 3, which provides that foreign individuals and enterprises and foreign-funded enterprises shall be accorded national treatment in respect of, *inter alia*, the procurement of inputs and goods and services necessary for production and the conditions under which their goods are produced, marketed or sold, in the domestic market and for export. The other is the Schedule of Specific Commitments on Services, which is attached to the Protocol in Annex 9. Again, the US did not specify the exact service sector that is at issue. In cases brought under the GATS, there is generally no requirement for

⁸⁶ Panel Report, *Indonesia – Certain Measures Affecting the Automobile Industry*, WT/DS54/R, WT/DS55/R, WT/DS59/R, WT/DS64/R and Corr.1, 2, 3, and 4, adopted 23 July 1998, DSR 1998:VI, 2201, at para 14.33.

⁸⁷ Appellate Body Report, *Canada – Certain Measures Concerning Periodicals*, WT/DS31/AB/R, adopted 30 July 1997, DSR 1997:I, 449, at para 34.

⁸⁸ See Yang Xueming, *Document 18 Does not Violate WTO Principles* (visited June 11, 2005) <<http://it.sohu.com/2004/03/20/82/article219518248.html>>.

⁸⁹ See e.g., Appellate Body Report, *Canada – Certain Measures Affecting the Automotive Industry*, WT/DS139/AB/R, WT/DS142/AB/R, adopted 19 June 2000, DSR 2000:VI, 2985, para 78.



the complaint to specify the sector at issue in its request for consultations.⁹⁰ This creates problem in the current case, however, as the Schedule of Specific Commitments of China does not specifically refer to IC design services. The current classification of services in the GATS is provided by the Services Sectoral Classification List drafted by the GATT Secretariat in 1991, which is based on the classification method of the UN Central Product Classification (CPC) system. Neither of them, however, explicitly mentions IC design. Looking at the sectors and sub-sectors that are explicitly provided for in the Schedule, IC design services seem to fall under engineering services (CPC 8672) or integrated engineering services (CPC 8673) of Sector A: Professional Services; or Sector B: Computer and Related Services. The US complaint concerns the discriminatory treatment between products designed abroad and those designed domestically. If such products are designed abroad, they might be manufactured in China or abroad. For those that are manufactured in China, even though they will not qualify for Article 48 rebate, they can still qualify for Article 41 rebate. Thus, there is no violation of national treatment obligation. For those that are manufactured abroad, the mode of supply for the design service is mode 2 – consumption abroad. In the “limitations on national treatment” column of its schedule, China does not inscribe any limitations as it puts “none” in all of the sectors mentioned above. Thus, for IC design services, China might have violated national treatment obligations.

After several rounds of consultations, China agreed to settle the case with the US by signing the Memorandum of Understanding between China and the United States Regarding China’s Value-Added Tax on Integrated Circuits on 14 July 2004. Under the terms of the settlement, China agreed to abolish the Article 41 rebate by 1 April 2005. Before the rebate is abolished, it would only be available to IC manufacturers which have already been certified as eligible for the rebates as of 14 July 2004. Also, China promised to issue a notice to revoke the Article 48 rebate by 1 September 2004, which shall take effect no later than 1 October 2004.⁹¹

Ironically, even though Document 18 was drafted with the intention of promoting the development of home-grown IC industry,⁹² its practical effect is exactly the opposite. The rebate schemes are based on the

⁹⁰ See e.g., the Request for Consultations of Antigua and Barbuda in *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, WT/DS285/1.

⁹¹ Joint Communication from China and the United States, WT/DS309/7.

⁹² Preamble of Notice of the State Council Regarding Issuance of Certain Policies to Promote the Development of the Software Industry and Integrated Circuit Industry.



effective tax rate, which equals the total tax payable divided by sales.⁹³ Because China provides 100 per cent VAT rebate for IC products exports, a firm have to sell at least 70-80 per cent of its products domestically and achieve a gross margin rate of 30 per cent or more in order to be able to enjoy the Article 41 rebate.⁹⁴ Since most of the Chinese firms export about 70-80 per cent of their products and have a low gross margin rate, very few of them could enjoy the rebates.⁹⁵ On the other hand, the foreign-invested IC firms in China focus on high-end products and thus have a much higher gross margin rate.⁹⁶ They also sell most of their products within China. As Document 18 applies to all firms irrespective of the ownership structure⁹⁷, most of the firms that were able to benefit from the rebate schemes are actually foreign-invested firms, such as Motorola.⁹⁸

Economically speaking, it seems sensible for China to agree to settle the case with the US. Legally speaking, China should not have settled the case so early with the US if it were indeed a faithful believer of aggressive legalism. After all, China could well follow the example of the US in the steel safeguards case and adopt the delay strategy to try to extort the maximum benefits. Unfortunately, China did not seem to feel comfortable with the idea of *"embroil all concerned in an intricate legal game"* or *"carefully trapping everything into the legitimate game of legal tactics"*.⁹⁹

3.3 The Sino-EC Dispute over Coke Export Quota

As we can see from the analysis in the last section, the VAT rebate case might not be a good case for China to hold on to aggressive legalism as China does not have either robust legal arguments or strong economic interests. The dispute between China and the EC over coke export quota, however, shows the deep reservations China has over aggressive legalism, even when it has the law on its side and the interests at stake are high.

⁹³ See e.g., *Behind the Tax Rebate Dispute* (visited August 3, 2005) <http://www.ccw.com.cn/news2/zl/htm2004/20040811_119N2.asp>.

⁹⁴ See *IC Dispute Escalated, the US Brought Lawsuit against China's Discriminative VAT Policy* (visited August 3, 2005) <<http://it.sohu.com/2004/03/20/82/article219518220.shtml>>.

⁹⁵ Id.

⁹⁶ Id.

⁹⁷ Article 52 of Notice of the State Council Regarding Issuance of Certain Policies Concerning the Development of the Software Industry and Integrated Circuit Industry.

⁹⁸ See *IC Dispute Escalated, the US Brought Lawsuit against China's Discriminative VAT Policy* (visited August 3, 2005) <<http://it.sohu.com/2004/03/20/82/article219518220.shtml>>.

⁹⁹ Pekkanen, *supra* note 1, at 732 (emphasis added).



Coke, which is produced by heating the coal in a high-temperature, oxygen-free furnace, is the main fuel used in making steel from iron ore. China is the world's top producer and exporter of coke. In 2003, the total global coke output 390 million Metric Tons (MT), with the Chinese production at 177 million MT, or 45 per cent of the world total production.¹⁰⁰ In the same year, China's coke export reached 14.7 million MT, nearly 60 per cent of the world's total.¹⁰¹ The EU, in particular, relies heavily on coke imports from China. In 2003 alone, the EU imported from China 4.4 million MT of coke, which is more than one-third of its total coke consumption.¹⁰²

On the other hand, the coke production process can cause serious pollution to the environment. Typically, two MT of coal can produce one MT of coke, while the rest turns into pollutants such as waste water, atmospheric emissions, and solid wastes. Among them are sulfur dioxide, which is the major cause for acid rain, and benzopyrene, which is one of the worst carcinogenic (cancer-causing) chemicals. In recent years, many coke plants were closed in the EU due to pressures from environmental protection groups. At the same time, however, the EU is home to four of the top ten steel manufacturers.¹⁰³ Thus, the European steel industry relies more and more on coke imports from China. This increasing gap between supply and demand also drives the price of coke in international markets from USD 56/MT FOB in 2000 to USD 400/MT FOB in 2004. The Chinese Government also started to study the pollution problem caused by coke-production. In July 2003, the Ministry of Commerce and the National Development and Reform Commission held a joint meeting on coke export with several industry associations. At the meeting, many experts suggested that the government limit coke exports to reduce pollution. On 1 January 2004, China announced that it would cut down its coke export quota by 26 per cent from twelve million tons for 2003 to nine million tons to meet the rising demand from its own booming steel and power industries.¹⁰⁴ The EU began to worry that it would not have enough coke for its domestic steel industries. On 31 March 2004, the EU asked China to abolish the coke export quota, or it would bring the case to the WTO. On 9th May 2004, the EU unilaterally announced a five-day deadline for the Chinese to

¹⁰⁰ China Metals Report Weekly, 8 June 2004, Tuesday.

¹⁰¹ China Metals Report Weekly, 8 June 2004, Tuesday.

¹⁰² China Metals Report Weekly, 8 June 2004, Tuesday.

¹⁰³ According to the International Iron and Steel Institute, of the top ten steel firms in 2003, four of them are EC firms. They are Arcelor (Luxemburg), LNM Group (Netherlands), Corus Group (UK/Netherlands), and ThyssenKrupp (Germany) (visited August 3, 2005) <<http://www.worldsteel.org/media/wsif/wsif2004.pdf>>.

¹⁰⁴ Xinhua News Agency, 24 May 2004, Monday.



get rid of the quota, otherwise it would initiate a complaint at the WTO. The deadline was later extended to 28th May 2004. After extensive negotiations, the EU announced on 28 May 2004 that it had secured a last-minute deal guaranteeing coke imports from China, removing the imminent threat of a WTO complaint. Under the agreement, the European steel industry would get at least 4.5 million MT of coke from China in 2004, the same quantity it imported in 2003. China also agreed to abolish the fee for the export permit, and this would reduce the price of coke from USD 450/MT to USD 250/MT.

The EU did not specify how the Chinese export quota violated the WTO rules. Of all WTO provisions, GATT Article XI.1 seems to provide the strongest basis for the EU complaint. The article reads:

“Article XI: General Elimination of Quantitative Restrictions

1. No prohibitions or restrictions other than duties, taxes or other charges, whether made effective through quotas, import or export licences or other measures, shall be instituted or maintained by any contracting party on the importation of any product of the territory of any other contracting party or on the exportation or sale for export of any product destined for the territory of any other contracting party.”

General elimination of quantitative restrictions is one of the most fundamental principles of the GATT and WTO. In *Turkey – Textiles*, the panel elaborated on the systemic significance of Article XI in the GATT framework by noting that:

“The prohibition on the use of quantitative restrictions forms one of the cornerstones of the GATT system. A basic principle of the GATT system is that tariffs are the preferred and acceptable form of protection. Tariffs, to be reduced through reciprocal concessions, ought to be applied in a non-discriminatory manner independent of the origin of the goods (the ‘most-favoured-nation’ (MFN) clause). Article I, which requires MFN treatment, and Article II, which specifies that tariffs must not exceed bound rates, constitute Part I of GATT. Part II contains other related obligations, inter alia to ensure that Members do not evade the obligations of Part I. Two fundamental obligations contained in Part II are the national treatment clause and the prohibition against quantitative restrictions. The prohibition against quantitative restrictions is a reflection that tariffs are GATT’s border protection



‘of choice’. Quantitative restrictions impose absolute limits on imports, while tariffs do not. In contrast to MFN tariffs which permit the most efficient competitor to supply imports, quantitative restrictions usually have a trade distorting effect, their allocation can be problematic and their administration may not be transparent.”¹⁰⁵

At the same time, the panel also acknowledged that GATT contracting parties have for many years failed to respect completely this obligation.¹⁰⁶ From early in the GATT, in sectors such as agriculture, textiles and clothing, quantitative restrictions were maintained and even increased.¹⁰⁷ Due to the prevalence of the quantitative restrictions, certain contracting parties were even of the view that quantitative restrictions had gradually been tolerated and accepted as negotiable and that Article XI could not be and had never been considered to be, a provision prohibiting such restrictions irrespective of the circumstances specific to each case.¹⁰⁸ This argument has been rejected by the panel in *EEC – Imports from Hong Kong*.¹⁰⁹ Also, during the Uruguay Round, the participants have agreed to phase-out quantitative restrictions in the sectors of agriculture and textiles and clothing.¹¹⁰ The WTO agreements, however, still retain many exceptions to this rule.

The first exception is in the paragraph immediately following Article XI.1, which provides:

“2. The provisions of paragraph 1 of this Article shall not extend to the following:

- (a) Export prohibitions or restrictions temporarily applied to prevent or relieve critical shortages of foodstuffs or other products essential to the exporting contracting party;
- (b) Import and export prohibitions or restrictions necessary to the application of standards or regulations for the classification, grading or marketing of commodities in international trade;

¹⁰⁵ Panel Report, *Turkey – Restrictions on Imports of Textile and Clothing Products*, WT/DS34/R, adopted 19 November 1999, as modified by the Appellate Body Report, WT/DS34/AB/R, DSR 1999:VI, 2363, at para. 9.63.

¹⁰⁶ *Id.* at para 9.64.

¹⁰⁷ *Id.*

¹⁰⁸ *Id.*

¹⁰⁹ *Id.*

¹¹⁰ Panel Report, *Turkey – Restrictions on Imports of Textile and Clothing Products*, WT/DS34/R, adopted 19 November 1999, as modified by the Appellate Body Report, WT/DS34/AB/R, DSR 1999:VI, 2363, at para 9.65.



- (c) Import restrictions on any agricultural or fisheries product, imported in any form, necessary to the enforcement of governmental measures which operate:
- (i) to restrict the quantities of the like domestic product permitted to be marketed or produced, or, if there is no substantial domestic production of the like product, of a domestic product for which the imported product can be directly substituted; or
 - (ii) to remove a temporary surplus of the like domestic product, or, if there is no substantial domestic production of the like product, of a domestic product for which the imported product can be directly substituted, by making the surplus available to certain groups of domestic consumers free of charge or at prices below the current market level; or
 - (iii) to restrict the quantities permitted to be produced of any animal product the production of which is directly dependent, wholly or mainly, on the imported commodity, if the domestic production of that commodity is relatively negligible."

In this case, China can argue that its restrictions fall under 2(a) as "export prohibitions or restrictions temporarily applied to prevent or relieve critical shortages of foodstuffs or other products essential to the exporting contracting party". Coke is not foodstuff, but it may well qualify as "other products essential to the exporting contracting party". Neither the GATT nor the WTO panels have elaborated on the exact meaning of "essential products". According to the Preparatory Committee, however, the standard seems to be relative as it noted that "for the purposes of this provision the importance of any product should be judged in relation to the particular country concerned".¹¹¹ Coal is widely used in China for heating and electricity generation. In 2003, for example, coal generated 84 per cent of the electricity in China. Thus, coal is "essential" for China. Because one needs two tons of coal to make one ton of coke, the increase in coke production will also lead to the "critical shortage" of coal as an "essential product". Steel is an "essential product" for many industries, and one needs 0.8 tons of coke to make one ton of steel. Thus, the increase in coke export will also lead to the "critical shortage" of steel as an "essential product". Also, coke is an "essential product" for the steel industry, the increase in coke export

¹¹¹ 51EPCT/141, P.2, as cited in *Guide to GATT Law and Practice* (electronic edition).



will also cause the “critical shortage” of coke as an “essential product” in the domestic market. To sum up, unless China imposes export restrictions on coke, it would have to face the “critical shortage” of at least three products, ie, coal, steel and coke.

One problem with this exception is that it can be only “temporarily applied”. China has been maintaining the export restriction since the Ministry of Foreign Trade and Economic Co-operation and China Commodity Inspection Bureau issued the Interim Rules on the Export Control of Coke in 1995. Thus, it might be hard for China to argue that such restriction is temporary.

Also, even if the coke export restriction can be justified under Article XI.2.(a), it must be administered in a non-discriminatory way according to Article XIII. As the current export quota applies to all countries, it probably satisfies Article XIII.

The second exception is the general exceptions clause under GATT Article XX, which reads:

“Article XX: General Exceptions

Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures:

- (a) necessary to protect public morals;
- (b) necessary to protect human, animal or plant life or health;
- (c) relating to the importations or exportations of gold or silver;
- (d) necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Agreement, including those relating to customs enforcement, the enforcement of monopolies operated under paragraph 4 of Article II and Article XVII, the protection of patents, trade marks and copyrights, and the prevention of deceptive practices;
- (e) relating to the products of prison labor;

- (f) imposed for the protection of national treasures of artistic, historic or archaeological value;
- (g) relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption;
- (h) undertaken in pursuance of obligations under any intergovernmental commodity agreement which conforms to criteria submitted to the Contracting Parties and not disapproved by them or which is itself so submitted and not so disapproved;
- (i) involving restrictions on exports of domestic materials necessary to ensure essential quantities of such materials to a domestic processing industry during periods when the domestic price of such materials is held below the world price as part of a governmental stabilization plan; Provided that such restrictions shall not operate to increase the exports of or the protection afforded to such domestic industry, and shall not depart from the provisions of this Agreement relating to non-discrimination;
- (j) essential to the acquisition or distribution of products in general or local short supply; Provided that any such measures shall be consistent with the principle that all contracting parties are entitled to an equitable share of the international supply of such products, and that any such measures, which are inconsistent with the other provisions of the Agreement shall be discontinued as soon as the conditions giving rise to them have ceased to exist. The Contracting Parties shall review the need for this sub-paragraph not later than 30 June 1960."

In *US-Gasoline*, the Appellate Body stated that Article XX requires a two-tier analysis: first, the measure at issue must come under one of the particular exceptions – paragraphs (a) to (j) – listed under Article XX; second, it must also satisfy the requirements imposed by the opening clauses (chapeau) of Article XX.¹¹²

Let us start with the first step. Of the two possible exceptions, five might be relevant in the present case.

¹¹² Appellate Body Report, *United States – Standards for Reformulated and Conventional Gasoline*, WT/DS2/AB/R, adopted 20 May 1996, DSR 1996:I, 3, at p. 22.

¹¹³ Panel Report, *United States – Standards for Reformulated and Conventional Gasoline*, WT/DS2/R, adopted 20 May 1996, as modified by the Appellate Body Report, WT/DS2/AB/R, DSR 1996:I, 29, at para 6.20.



The most obvious one is (b), ie measures “necessary to protect human, animal or plant life or health”. According to the Panel in *US-Gasoline*, the party invoking the exception has to establish the following elements:

“(1) that the policy in respect of the measures for which the provision was invoked fell within the range of policies designed to protect human, animal or plant life or health;

(2) that the inconsistent measures for which the exception was being invoked were *necessary* to fulfill the policy objective”.¹¹³

The first element seems to be rather straightforward and can be established with the relevant scientific evidence. According to prior WTO cases, the Member invoking the exception enjoys a wide margin of discretion. For example, the Appellate Body stressed in *EC-Asbestos* that: “it is undisputed that WTO Members have the right to determine the level of protection of health that they consider appropriate in a given situation.”¹¹⁴ The Appellate Body further pointed out that: “a Member may also rely, in good faith, on scientific sources which, at that time, may represent a divergent, but qualified and respected, opinion. A Member is not obliged, in setting health policy, automatically to follow what, at a given time, may constitute a majority scientific opinion.”¹¹⁵ As the author stated earlier, the coke production process can cause severe pollution to the environment, including the air and water. The health risks such pollution might pose to humans, animal and plants have been well established. In *US-Gasoline*, for example, the US argued that: “[t]oxic air pollution was a cause of cancer, birth defects, damage to the brain or other parts of the nervous system, reproductive disorders and genetic mutation. It could affect not only people with impaired respiratory systems, but healthy adults and children as well.”¹¹⁶ In that case, both the complainant and the panel agree that a policy to reduce air pollution would fall within the range of policies concerning the protection of human, animal and plant life or health mentioned in Article XX(b).¹¹⁷ In

¹¹⁴ Appellate Body Report, *European Communities – Measures Affecting Asbestos and Asbestos-Containing Products*, WT/DS135/AB/R, adopted 5 April 2001, DSR 2001:VII, 3243, at para. 168.

¹¹⁵ *Id.* paras. 177–178.

¹¹⁶ Panel Report, *United States – Standards for Reformulated and Conventional Gasoline*, WT/DS2/R, adopted 20 May 1996, as modified by the Appellate Body Report, WT/DS2/AB/R, DSR 1996:I, 29, at para 3.39.

¹¹⁷ Panel Report, *United States – Standards for Reformulated and Conventional Gasoline*, WT/DS2/R, adopted 20 May 1996, as modified by the Appellate Body Report, WT/DS2/AB/R, DSR 1996:I, 29, at para 6.21.

¹¹⁸ Panel Report, *Thailand – Restrictions on Importation of and Internal Taxes on Cigarettes* (BISD 37S/200), adopted 20 February 1990, at para 75.



the current case, the fact that the EC itself has closed many coke factories also provides further evidence supporting that restricting coke production is in the interests of protecting human, animal and plant life or health. Thus, China can easily prove the first element. The second element seems to be harder to establish. According to the panel in *Thailand-Cigarettes*, "import restrictions ... could be considered to be "necessary" in terms of Article XX(b) only if there were no alternative measure consistent with the [GATT], or less inconsistent with it, which [the Member concerned] could *reasonably be expected to employ to achieve its health policy objectives*."¹¹⁸ In that case, Thailand prohibits imports of foreign cigarettes on the grounds of protecting human health, while not prohibiting domestic cigarettes manufacturers to produce cigarettes at all. The panel struck down the measure as unnecessary because Thailand can be reasonably expected to adopt another GATT-consistent measure to achieve the same purpose, ie, prohibits both imported and domestically produced cigarettes. In the current case, as China only restricts coke exports while not prohibiting or restricting domestic coke production at the same time, it might be hard to argue that such export restrictions are necessary. One might argue that domestic restriction on coke production is much more difficult to administer than simply restricting exports and thus can not be considered to be a "reasonably available" measure. This argument is unlikely to succeed, however, as the Appellate Body has already made clear in *EC-Asbestos* that "an alternative measure did not *cease* to be 'reasonably' available simply because the alternative measure involved *administrative difficulties* for a Member".¹¹⁹

The next possible exception is (d), ie measures "necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Agreement". As the Appellate Body stated in *Korea-Beef*, the Member which invokes Article XX(d) must demonstrate that two requirements are met: "[f]irst, the measure must be one designed to 'secure compliance' with laws or regulations that are not themselves inconsistent with some provision of the GATT 1994. Second, the measure must be 'necessary' to secure such compliance".¹²⁰ As with (b), the key is the meaning of the word "necessary". In *Korea-Beef*, the Appellate Body starts with the ordinary meaning of the word "necessary", which, according to the New Shorter Oxford English Dictionary, "normally

¹¹⁹ Appellate Body Report, *European Communities – Measures Affecting Asbestos and Asbestos-Containing Products*, WT/DS135/AB/R, adopted 5 April 2001, DSR 2001:VII, 3243, at para. 169.

¹²⁰ Appellate Body Report, *Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, WT/DS161/AB/R, WT/DS169/AB/R, adopted 10 January 2001, DSR 2001:I, 5, at para. 157.



denotes something ‘that cannot be dispensed with or done without, requisite, essential, needful’.¹²¹ The Appellate Body further notes that Black’s Law Dictionary cautions that:

“[t]his word must be considered in the connection in which it is used, as it is a word susceptible of various meanings. It may import absolute physical necessity or inevitability, or it may import that which is only convenient, useful, appropriate, suitable, proper, or conducive to the end sought. It is an adjective expressing degrees, and may express mere convenience or that which is indispensable or an absolute physical necessity.”¹²²

With these definitions in mind, the Appellate Body explains that “as used in the context of Article XX(d), the reach of the word ‘necessary’ is not limited to that which is ‘indispensable’ or ‘of absolute necessity’ or ‘inevitable’”.¹²³ It refers, instead, “to a range of degrees of necessity. At one end of this continuum lies ‘necessary’ understood as ‘indispensable’; at the other end, is ‘necessary’ taken to mean as ‘making a contribution to’.”¹²⁴ According to the Appellate Body, a “necessary” measure is, in this continuum: “located significantly closer to the pole of ‘indispensable’ than to the opposite pole of simply ‘making a contribution to’.”¹²⁵ Realizing that such philosophical discourse does not offer much-needed practical guidance to the “necessity” question, the Appellate Body further points out that “[i]n appraising the ‘necessity’ of a measure in these terms, it is useful to bear in mind the context in which ‘necessary’ is found in Article XX(d).”¹²⁶ According to the Appellate Body: “determination of whether a measure, which is not ‘indispensable’, may nevertheless be ‘necessary’ within the contemplation of Article XX(d), involves in every case a process of weighing and balancing a series of factors which prominently include the contribution made by the compliance measure to the enforcement of the law or regulation at issue, the importance of the common interests or values protected by that law or regulation, and the accompanying impact of the law or regulation on imports or exports.”¹²⁷

¹²¹ Id. at para 160.

¹²² Id.

¹²³ Appellate Body Report, *Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, WT/DS161/AB/R, WT/DS169/AB/R, adopted 10 January 2001, DSR 2001:I, 5, at para 161.

¹²⁴ Id.

¹²⁵ Id.

¹²⁶ Appellate Body Report, *Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, WT/DS161/AB/R, WT/DS169/AB/R, adopted 10 January 2001, DSR 2001:I, 5, at para 162.

¹²⁷ Id. at paras 162-164.



As we can see from the analysis above, even though both paragraphs (b) and (d) use the same word “necessary”, their meanings are quite different. In some way, paragraph (b) can be regarded as one of the specific examples of paragraph (d). To paraphrase paragraph (d), paragraph (b) can be restated as measures “necessary to secure compliance with laws or regulations which are designed to protect human, animal or plant life or health”. Applying the “weighing and balancing” test in (d), the “interests or values” to be protected by (b) is of utmost importance. Thus, such measure does not have to be “indispensable” or “of absolute necessity”; rather, so long as there is no other reasonably available WTO-consistent alternative, the measure shall be considered necessary.

Applying the two-step test to the current case, the export restriction must be designed to “secure compliance” with laws or regulations that are not themselves inconsistent with some provision of the GATT 1994. If the restriction is drafted as a simple export quota, it will be hard to invoke the exception in (d) as the law itself is not consistent with GATT Article XI. With some proper legislation-drafting technique, however, the export restriction may be converted into a pollution disposal and treatment fee scheme for coke-production. The scheme works as follows: for coke for domestic consumption, the fee will be shared equally between the producer and the consuming firm; for export coke, the entire fee will be collected from the producer as it is too burdensome to collect the consuming firm’s share. The difference in treatments for domestically-consumed coke and export coke is based on the administrative difficulties in collecting the fee from the buyers abroad. As mentioned earlier in the discussions on paragraph (b), administrative difficulties cannot be used to justify the measure as necessary under (b). The standard under paragraph (d), however, includes a range of degrees of necessity. Thus, whether administrative difficulties can be used to justify the measure as necessary under (d) is determined by a case-by-case analysis. In the current case, as the protection of human, animal or plant life or health is a very important common interest, administrative difficulties should be sufficient to justify the measure as necessary. Also, one can convert the quota into a staggered disposal fee: the higher the amount exported, the higher the fee will be. With proper calculation, such fee can be set in such a way that it will not be commercially viable for the producer to export once the amount exported exceeds a certain level. At the same time, China should also amend its environmental and resource protection laws to include the relevant provisions on the pollution disposal and treatment fee. This will change the purpose of such measure from restricting trade to environmental protection and make it easier to invoke the exception under paragraph (d).



The third option is (g), ie measures “relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption”. The key here is the term “exhaustible natural resources”. The Appellate Body noted in *US-Shrimp* that “petroleum, iron ore and other non-living resources” are classic examples of “exhaustible natural resources”.¹²⁸ At the same time, the concept “is not ‘static’ in its content or reference but is rather ‘by definition, evolutionary’”.¹²⁹ Thus, the term shall be interpreted “in the light of contemporary concerns of the community of nations about the protection and conservation of the environment”.¹³⁰ With this in mind, the Appellate Body pointed out that “living species, though in principle, capable of reproduction and, in that sense, ‘renewable’, are in certain circumstances indeed susceptible of depletion, exhaustion and extinction, frequently because of human activities... [Therefore, even] [l]iving resources can be ‘exhaustible natural resources’”.¹³¹ In the current case, coke is an exhaustible resource. Because it is made artificially from coal, however, it itself is not a “natural” resource. Nonetheless, as one needs two tons of coal to produce one ton of coke, the coke production process will reduce the amount of coal, which is clearly an “exhaustible natural resource”.¹³² Furthermore, the coke production process will pollute both the air and underground water. In *US-Gasoline*, the panel has already determined that clean air is an “exhaustible natural resource”. Along the same line of reasoning, underground water should also be recognized as an “exhaustible natural resource”. Thus, China can probably cite the exception under paragraph (g) to protect “exhaustible natural resources” such as coal, air and water. Of course, China should also restrict the domestic production and consumption of coke in order to satisfy the requirements under (g).

The fourth exception available is (i), i.e. measures “involving restrictions on exports of domestic materials necessary to ensure essential quantities of such materials to a domestic processing industry during periods when the domestic price of such materials is held below the world price as part of a governmental stabilization plan; Provided that such restrictions shall not operate to increase the exports of or the protection

¹²⁸ Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, WT/DS58/AB/R, adopted 6 November 1998, DSR 1998:VII, 2755, at para. 128.

¹²⁹ *Id.* at para. 130.

¹³⁰ *Id.* at para. 129.

¹³¹ *Id.* at para. 128.

¹³² Panel Report, *United States – Standards for Reformulated and Conventional Gasoline*, WT/DS2/R, adopted 20 May 1996, as modified by the Appellate Body Report, WT/DS2/AB/R, DSR 1996:I, 29, at para 6.36.



afforded to such domestic industry, and shall not depart from the provisions of this Agreement relating to non-discrimination". Coke is a material necessary for steel-manufacturing, thus the restrictions on coke exports is necessary to ensure sufficient quantities of coke to the domestic steel industry. Currently, 35 per cent of the steel firms in China need to buy their coke from outside.¹³³ Also, steel itself is a necessary material for many other industries. The domestic industries have a huge demand for steel.¹³⁴ In order to fill such demand, they even have to import steel from abroad. Thus, such restriction is not applied "to increase the exports of or the protection afforded to such domestic industry".

The last exception is (j), ie measures "essential to the acquisition or distribution of products in general or local short supply". Currently coke is not in short supply domestically, but China can probably invoke this clause if such short supply does materialize.

Let us next look at the second requirement, ie "such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade". From its face, it appears that the chapeau refers to two different scenarios, ie "arbitrary or unjustifiable discrimination" or a "disguised restriction on international trade". The Appellate Body has made clear, however, that the two scenarios entail the same factors under consideration.¹³⁵ In *US-Shrimp*, the Appellate Body points out that, in order for a measure to be applied in a manner which would constitute "arbitrary or unjustifiable discrimination between countries where the same conditions prevail", three elements must exist: "[f]irst, the application of the measure must result in *discrimination*. Second, the discrimination must be *arbitrary* or *unjustifiable* in character. Third, this discrimination must occur *between countries where the same conditions prevail*"¹³⁶ In considering the three elements, the first question that comes

¹³³ *Chinese Coke: Suspense Abound in Exports to the EU* (visited 3 August 2005) <<http://www.dajingmao.com/sub/view.asp?id=1344>>.

¹³⁴ According to the International Iron and Steel Institute, China's steel output in 2003 was 22.8 per cent of the world's total production, while it consumes 27.2 per cent of the world's total production. See *World Steel in Figures 2004* (visited August 3, 2005) <<http://www.worldsteel.org/media/wsif/wsif2004.pdf>>.

¹³⁵ Appellate Body Report, *United States – Standards for Reformulated and Conventional Gasoline*, WT/DS2/AB/R, adopted 20 May 1996, DSR 1996:I, 3, at p. 25.

¹³⁶ Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, WT/DS58/AB/R, adopted 6 November 1998, DSR 1998:VII, 2755, at para 150.



to mind is whether the word “discrimination” here has the same meaning as the same word used in other GATT articles (eg Article III). The Appellate Body gave a negative answer in *US-Gasoline*. According to the Appellate Body: “[t]he provisions of the chapeau cannot logically refer to the same standard(s) by which a violation of a substantive rule has been determined to have occurred. To proceed down that path would be both to empty the chapeau of its contents and to deprive the exceptions in paragraphs (a) to (j) of meaning. Such recourse would also confuse the question of whether inconsistency with a substantive rule existed, with the further and separate question arising under the chapeau of Article XX as to whether that inconsistency was nevertheless justified. One of the corollaries of the ‘general rule of interpretation’ in the Vienna Convention is that interpretation must give meaning and effect to all the terms of a treaty. An interpreter is not free to adopt a reading that would result in reducing whole clauses or paragraphs of a treaty to redundancy or inutility.”¹³⁷ At the same time, however, the Appellate Body fails to announce a clear standard for determining “discrimination” under the chapeau of Article XX. Instead, it took a case-by-case approach. For instance, in *US-Shrimp*, the Appellate Body held that “discrimination” exists for the following reasons: a, “the application of the measure at issue does not allow for any inquiry into the appropriateness of the regulatory programme for the conditions prevailing in those exporting countries”;¹³⁸ b, “there is little or no flexibility in how officials make the determination for certification pursuant to [the US regulations]”;¹³⁹ c, “exporting Members applying for certification whose applications are rejected are denied basic fairness and due process”.¹⁴⁰ Thus, the “discrimination” question here relates more to the procedural justice than the substantive treatments. This is indeed confirmed by the recent *US-Gambling and Betting Services* case, where the panel noted that “the chapeau of Article XX of the GATT 1994 addresses not so much a challenged measure or its specific content, but rather the manner in which that measure is applied, with a view to ensuring that the exceptions of Article XX are not abused”.¹⁴¹ Another question is whether the expression “countries where the same conditions

¹³⁷ Appellate Body Report, *United States – Standards for Reformulated and Conventional Gasoline*, WT/DS2/AB/R, adopted 20 May 1996, DSR 1996:I, 3, at p. 23.

¹³⁸ Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, WT/DS58/AB/R, adopted 6 November 1998, DSR 1998:VII, 2755, at paras. 164–165.

¹³⁹ *Id.* at para. 177.

¹⁴⁰ *Id.* at paras. 180–181.

¹⁴¹ Panel Report, *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, WT/DS285/R, adopted 20 April 2005, as modified by the Appellate Body Report, WT/DS285/AB/R, at para 6.581.



prevail" refers only to the conditions between different exporting Members, or it also includes conditions between exporting Members and the importing Member concerned. In *US-Shrimp*, the Appellate Body held that both should be included.¹⁴² Applying the rules above to the current case, in order to satisfy the requirements under the chapeau, China should make its rule-making process more transparent, and also give other countries an opportunity to participate in such process. On the other hand, as most of the GATT/WTO cases concern import restrictions, it is arguable as to whether the same rules should also be applicable to the export restrictions, which is the situation in the current case.

Even though China could make some good legal arguments if the case did go to the WTO, China decided to settle the case in the end. This case provides interesting contrast with the *US-Steel Safeguard* case. In both cases, China has strong legal arguments and major economic interests. There are two major differences, however, between the two cases. In the *Coke* case, China was the respondent rather than the complainant. Also, in the same case, China was fighting alone against the EU, rather than working along with a team of other WTO Members. These two differences are what prompted China's decision to settle. China's decision also shows that it is not ready to embrace aggressive legalism yet.

4. Lessons for China

These three cases show a clear reluctance of China to make use of the WTO dispute settlement system. Will aggressive legalism always be beyond the Chinese? What are the pre-conditions before China can adopt aggressive legalism in the WTO? Drawing from the lessons of Japan and Korea, the following are the major factors which will determine China's future attitude towards the WTO dispute settlement system.

The first factor is a proper understanding of the nature of the WTO dispute settlement system. During the GATT era, the contracting parties often preferred the "pragmatism" approach of settling disputes by diplomatic means. Too much emphasis on the legalist nature of the dispute settlement process or the participation of lawyers might undermine this tradition or even endanger the diplomatic relationships of the parties. After the WTO was established at the conclusion of the

¹⁴² Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, WT/DS58/AB/R, adopted 6 November 1998, DSR 1998:VII, 2755, at para 150.



Uruguay Round, however, this perception has been changed once and for ever. The new Dispute Settlement Understanding explicitly provides that “requests for conciliation and the use of the dispute settlement procedures should not be intended or considered as contentious acts”.¹⁴³ Thus, the active use of the WTO dispute settlement system is not in conflict with China’s policy of peaceful development; instead, it should be an integral part of this policy. As discussed earlier, the major advantage of aggressive legalism is that it turns cross-border disputes from a difficult political, trade or diplomatic issue that might undermine the bilateral relationships of the countries involved into a legal issue that is embroiled in an intricate legal game. Instead of a sensitive issue that can be easily polarized by the popular press, the question now has become a highly technical legal game that is beyond the grasp of lay people. If the Member wins the case, the politicians can claim all the credit for having worked hard to achieve “real results”; if the Member loses the case, the lawyers, or more frequently, the “incompetent judges in Geneva”, will become easy scapegoats.

The second factor is the improvement of the dispute settlement system. Even though Japan and Korea have been contracting parties to the GATT since the 1950s and 1960s, they have for a long time been avoiding using the dispute settlement system as it suffered from systemic weakness. The WTO, however, establishes a nicely-crafted rule-oriented system for the settlement of trade disputes by improving the substantive aspects of the system with the new DSU. The new WTO dispute settlement system has been hailed by former Director General Mike Moore as the “Crown Jewel” of the WTO, and praised by scholars as one of the most effective mechanisms in the various international dispute settlement tribunals. Thus, the Chinese Government should make the best use of the new dispute settlement system to protect its interests.

The third factor is the availability of the expertise. Unless a Member has many experts who understand the intricacies of the WTO legal system, it could not participate in the dispute settlement process effectively. This problem, however, should be easy to solve as it does not require structural adjustment. There are two ways to build up the expertise. First, the Member could use foreign lawyers in its cases. For example, China retained a French law firm in the *US-Steel Safeguard* case. Second, the Member should also try to develop the capacity at home. This should not be limited to the training of government officials; rather,

¹⁴³ Article 3.10 of the DSU.



the government should also encourage lawyers as well as scholars and researchers to work on WTO-related issues. In practice, one of the most effective ways to build up the expertise is to encourage its citizens to work in the WTO Secretariat. Of the 630 current members of the WTO Secretariat, nationals from the EU, US, Canada, India and Australia account for more than two-thirds.¹⁴⁴ In the three main divisions responsible for most dispute settlement cases, ie Legal Affairs Division, Appellate Body Secretariat and Rules Division, their share is even higher. It is no wonder, therefore, that these Members are among the most active users of the WTO dispute settlement system. Of course, as stated in Article VI.4 of the WTO Agreement, the staff of the Secretariat, in the discharge of their duties, shall not seek or accept instructions from any government or any other authority external to the WTO. Furthermore, they shall refrain from any action which might adversely reflect on their position as international officials, and the Members of the WTO shall also respect the international character of their responsibilities and shall not seek to influence them in the discharge of their duties. The WTO also has strict Rules of Conduct for those Secretariat staff who are involved in the settlement of disputes.¹⁴⁵ None of the rules seem to apply, however, to those who have terminated employment relationship with the WTO. Indeed, the WTO Secretariat is just like a revolving door, where people constantly come in and out, while most keep working on WTO-related issues in different capacities even after they have left the Secretariat. One recent example is Mr Hyun Chong Kim, who left the Secretariat to become the Korean Minister of Trade after having worked for several years in the Appellate Body Secretariat and the Legal Affairs Division. Since China acceded to the WTO in 2001, several Chinese nationals have joined the WTO Secretariat. In recent years, many Chinese government officials and lawyers also participated in the WTO dispute settlement process in various ways. They will be an important pool of resources for China's participation in the WTO dispute settlement system.

The fourth factor is the trade balance. As we can see from the experience of Japan and Korea, a Member which maintains a trade surplus against its trade partners generally finds it awkward to aggressively use the dispute settlement system to deal with the disputes with its trade partners. Instead, it often finds it a better strategy to keep a low profile

¹⁴⁴ *The WTO: Secretariat And Budget, Overview of the WTO Secretariat, Table of regular staff by nationality*, (visited 3 August 2005) <http://www.wto.org/english/thewto_e/secre_e/intro_e.htm>.

¹⁴⁵ *Rules of conduct for the understanding on rules and procedures governing the settlement of disputes*, WT/DSB/RC/1, 11 December 1996.



and avoid resorting to the dispute settlement system as much as possible. This is understandable as a country with a high trade surplus are usually easy scapegoats for the domestic problems of its trade partners and a strategy of aggressive legalism can entail significant political costs for such country. On the other hand, when the trade surplus is turned into deficient, the domestic pressures will become stronger for such Member, making it more willing to take a more legalistic approach. For China, even though it has always been maintaining a trade surplus, the share of such surplus in the total import and export has been shrinking.¹⁴⁶ Also, in 2004, the imports have grown 36 per cent, which is higher than the export growth rate of 35.4 per cent. this is what is bound to happen after China's accession to the WTO: on the one hand, China has agreed to progressively lower its tariff level and this would lead to the increase of import; on the other hand, several discriminatory clauses in China's Accession Protocol and Working Party Report have made it easier for other Members to impose restrictions against Chinese exports. Indeed, it is only a matter of time for China's trade surplus to turn into trade deficient. Once China no longer maintains trade surplus any more, it will probably become more active in using the WTO dispute settlement system.

¹⁴⁶ China's trade surplus in 2002 is USD 30.35 billion, or 4.89% of the total trade of USD 620.79 billion . For 2002 it is USD 25.54 billion, or 2.97% of the total trade of USD 851.21 billion . It is USD 31.98 billion in 2004, or 2.77% of USD 1154.74 billion. All figures are taken from the website of the Ministry of Commerce of China (last visited 3 August 2005) < <http://www.mofcom.gov.cn>>.