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Negotiating Group on Dispute Settlement

CONCEPT, FORMS AND EFFECTS OF ARBITRATION

Note by the Secretariat

1. At its meeting of 20 November 1987, the Group requested the secretariat to prepare a background paper clarifying the concepts, different kinds and legal effects of arbitration in order to assist the Group in its further deliberations (MTN.GNG/NG13/5, para. 6). Part I of this paper attempts to clarify conceptual issues. Part II gives a survey of procedural issues to be taken into account in the regulation of arbitration. Part III briefly summarizes and compares proposals made so far by contracting parties for the use of arbitration in GATT. The paper has been prepared on the sole responsibility of the secretariat and does not commit any delegation.

1. Conceptual Issues

2. The various techniques and institutions available to states for the peaceful settlement of disputes are usually subdivided into the so-called "diplomatic" and the "legal" means of settlement of "disputes" (i.e. a specific disagreement concerning a matter of fact, law or policy in which a claim or assertion by one party is met with refusal, counter-claim or denial by another). Each of these dispute settlement methods uses specific techniques designed to fit different situations and to maximize the chances of dispute settlement by successive or alternative use of different methods. While, in GATT practice, the various terms of art are often not clearly distinguished, it might be useful to be aware of the terminology used in state practice outside GATT and in the literature. The "diplomatic" means of dispute settlement, all of which are available also in GATT practice, are generally defined and classified as follows:

A. Negotiation. It continues to be the basic means of resolving disputes peacefully and serves the purpose of achieving agreed solutions among the parties to the dispute. It is usually distinguished from other means of dispute settlement by the absence of a neutral third party which could suggest or even impose a solution. A legal duty to negotiate entails for the parties to the dispute an "obligation so to conduct themselves that the negotiations are meaningful" (ICJ Reports, 1969, p. 47). Negotiations to prevent disputes from arising are referred to as "consultation". The precise legal definition of the term "negotiation" has posed a problem in various international court proceedings, when the jurisdiction of the court was confined to "disputes incapable of settlement by negotiation" (e.g. ICJ Reports, 1963, pp. 15, 123).

B. Good Offices. The intervention of a third party in disputes among states with the aim of contributing to their settlement can take a number of different forms such as "good offices", "mediation", "inquiry" and "conciliation". The term "good offices" is used when the involvement of one or more states or of an international organization in a dispute between other states is confined to encouraging the disputing states to resume negotiations and/or to provide them with additional channels of communication. Good offices may be offered by a state or international organization within its sphere of competence on their own initiative or may be requested by one or both parties to the dispute.

C. Mediation. It differs from good offices by the more active participation of the mediator (a state, international organization or individual) who is authorized and expected to transmit and interpret each party's proposals to the other and to advance his own proposals informally on the basis of the information supplied by the parties rather than his own investigations. While the mediator may act on his own initiative or in response to a request from one or both parties to the dispute, mediation can take place only with the consent of the disputing parties. The proposals do not bind the parties which retain control of the dispute. They may be based not only on existing law but also on considerations ex aequo et bono. In addition to proposing compromises, the mediator may offer also other services (e.g. financial aid for carrying out the compromise).

D. Inquiry and "fact-finding" are methods of ascertaining disputed issues of fact by requesting a disinterested third party to provide the disputing parties with an objective assessment. The disputing parties may agree in advance to accept the report of the impartial body entrusted with the establishment of facts as binding.

E. Conciliation can take place at the request of one or both disputing parties and is distinguished from mediation by the fact that the third-party intervention is put on a formal legal and institutionalized basis (usually a conciliation commission). The members of conciliation bodies usually act as independent persons in their personal capacity and not as functionaries of their state or organization. The rules of conciliation procedures tend to be more formal than those of mediation and are often patterned after those used in arbitration proceedings. Conciliation bodies are usually requested to establish the facts, examine the claims of both parties, take all other relevant factors into account (including the legal situation), and to submit legally non-binding proposals for a possible settlement. In spite of many common features, the practice of individual conciliation commissions exhibits significant differences of approach depending on the instrument setting them up, the requests by the parties and on how the conciliators have perceived their task.

Confidentiality has been the general rule in conciliation proceedings because it is easier for governments to offer concessions without publicity. Since the conciliation proposals remain non-binding even in cases where law has been a major consideration, conciliation reports have sometimes been submitted subject to a proviso that "the opinion of the Commission on points of law may not be invoked by the parties before any tribunal, judicial or arbitral". If conciliation proposals are accepted, conciliation commissions usually draw up a procès-verbal recording the fact of conciliation and setting out the terms of the settlement. Even though the possibility of conciliation has been provided for in numerous multilateral and more than 200 bilateral treaties over the past 65 years, only about 20 formal conciliation proceedings have been held (i.e. not including informal conciliation within international organizations).

3. The "diplomatic" means of dispute settlement are characterized by the flexibility of the procedures, the control over the dispute by the parties, their freedom to accept or reject a proposed settlement, the possibility of avoiding "victor-loser-situations" with their repercussions on the prestige of the parties, the only limited influence of legal considerations, and the often larger influence of the current political processes in, and relative political weight of, each party. The "legal" means of dispute settlement through arbitration and courts, which are also available in GATT practice (see, e.g., GATT Article X:3, b), tend to be employed when the parties want to obtain "rule-oriented", binding decisions in conformity with their mutually agreed long-term obligations and interests (as defined in multilaterally agreed legal rules of a permanent nature) and prefer to avoid the various risks involved in "diplomatic" means of dispute settlement (such as dependence on the consent and good will of the defendant, bilateral ad hoc solutions possibly reflecting the relative power of the parties rather than the merits of their case, a weakening effect on the legal rules and on their uniform, multilateral interpretation). While judicial settlement involves the reference of a dispute to a national or international standing tribunal, arbitration allows the parties themselves to appoint arbitrators of their own choice and confidence, to define the scope of the "dispute" and of the jurisdiction of the tribunal, and to determine the applicable procedures and substantive rules for the settlement of the dispute (or series of disputes).

II. Forms and Effects of Arbitration

4. Arbitration can be defined as the process of resolving disputes on the basis of respect for law through decisions binding upon the disputant parties by arbitrators appointed by the parties to hear a particular case submitted by the parties. Arbitration presupposes (A) an agreement among the parties to the dispute, which (B) defines the form of arbitration, (C) the selection of arbitrators, (D) the terms of reference, (E) the basis of the decision, and (F) the effect of the award.

A. Arbitration Clauses

5. Arbitration clauses ("compromissory clauses") providing for dispute settlement through arbitration can be agreed upon either before or after differences arise between the parties. An agreement to submit an already existing, particular dispute to the jurisdiction of an arbitral body or court is called "ad hoc compromis". An agreement submitting all or definite classes of disputes, which may arise between the parties, to an arbitral institution or court is called a "general", "abstract" or "anticipated compromis". In the latter case, the general arbitration agreement needs to be implemented through an additional "implementing compromis" or "protocol of submission". There are no special requirements concerning the form of a compromis, as is true for international agreements in general, but normally they are in writing. The contents of a compromis depend on the particular circumstances of the case and usually regulate the subject-matter of the dispute, the form of the arbitration, the manner of appointing arbitrators, the applicable law and procedures which must be compatible with the nature of arbitration and with any mandatory rules of an already existing arbitration body to which the dispute is being referred. The compromis may also refer to the various existing model rules of arbitration so as to obviate or remedy possible delays. The parties to a "general compromis" (e.g. an arbitration clause stating that a dispute "shall be referred to arbitration") are under an obligation to negotiate in good faith for the conclusion of an "implementing compromis", once a concrete dispute arises and the arbitration clause is being invoked. Similarly, the parties to an ad hoc or implementing compromis are under a legal obligation to cooperate bona fide in the setting up of the arbitral body. The compromis may include provisions designed to secure the implementation of a compromis also in a situation where one party refuses to cooperate (e.g. authorization of an existing arbitral or other body to complete itself the compromis, or recognition of a right of each party to seize an existing arbitral tribunal unilaterally).

6. Arbitration clauses in treaties often provide for recourse to arbitration only after the exhaustion of other means of dispute settlement. Some arbitration clauses permit the unilateral appeal to an arbitration body, or provide for the possibility of interim measures of protection, or are optional and open to reservations, or grant also private persons the right to file claims to "mixed arbitral tribunals".

B. Forms of Arbitration

7. Disputes may be arbitrated by an ad hoc or by a permanent tribunal or "mixed commission" usually composed of an uneven number of arbitrators (mostly three or five) with the power to decide by majority vote. There is also a long-established practice of referring a dispute to a foreign head of state or another influential or specially qualified personality for arbitration. Ad hoc tribunals are set up after a dispute has arisen with

the aim of settling that particular dispute. The term "permanent arbitral tribunal" is used for arbitration bodies provided for in agreements to decide disputes which may arise in future between the parties. The parties may provide for compulsory jurisdiction of such permanent tribunals so that either party may invoke the tribunal's jurisdiction unilaterally without need for an additional "implementing compromis". The arbitration procedures are often left to be determined by the tribunal itself.

C. Selection of Arbitrators

8. Even though arbitration bodies may consist of a single arbitrator appointed by common agreement between the parties, they are usually composed of one or two "national" members appointed by each side and a "neutral" member serving as president and chosen either by agreement among the parties or by a procedure laid down in the arbitration agreement. If the arbitration clause neither identifies the arbitrators nor lays down the procedure to be followed for their choice (e.g. appointment of the "neutral" arbitrator by the other members of the tribunal or by a disinterested third personality), the pertinent provisions of Title IV.3 of the Hague Conventions for the Pacific Settlement of International Disputes of 1899 and 1907 are applicable among states which have ratified the conventions.

D. Terms of Reference

9. The jurisdiction of the arbitral body is defined by the "compromis" and limited to those questions referred to it by agreement between the parties. It may extend to all kinds of disputes. According to Article 84:2 of the 1907 Hague Convention for the Pacific Settlement of International Disputes, third states have the right to intervene in a pending arbitration if it concerns the interpretation of a treaty to which they are parties; in such a case, the parties to the arbitration are under an obligation to inform all signatories of the treaty in good time.

E. Applicable Law and Procedures

10. The parties can also determine the rules and procedures which the tribunal shall apply in making its decision. Such directives by the parties limit the authority of the arbitration body and must always be respected. The applicable rules may be not only international and/or municipal law but also "equitable considerations" of various kinds. If the parties' directives are unclear or silent on the applicable law, the tribunal has to determine the principles upon which the decision is to be based. When the parties request an arbitration *ex aequo et bono*, the arbitrator acts no longer merely as "adjudicator" (i.e. applying existing rules) but assumes also "law-creating" functions for the case in hand (but also arbitration according to law is hardly ever simply a mechanical process of applying rules). If the procedures to be followed by the arbitral tribunal have not been specifically determined by the parties, the procedural provisions of the Hague Conventions for the Pacific Settlement of International Disputes apply to signatories.

F. Effects of the Award

11. Arbitration awards are only binding on the parties to the proceedings. However, according to Article 86 of the 1907 Hague Convention for the Pacific Settlement of International Disputes, the interpretation in an arbitration award of a multilateral treaty provision is binding also on other signatories if they exercise their right to intervene in the proceedings. Once the award is notified to the parties and enters into effect, the award settles the dispute finally and must be carried out in good faith unless the terms of the arbitration reserve the right to take further proceedings (e.g. a request for an interpretation of the award, for its revision on the ground of discovery of new evidence, or an appeal against the award on the ground of excess of jurisdiction by the tribunal). In rare situations, a party may claim that an award has not become effective because of nullity (e.g. in case of transgression of a basic procedural rule).

III. Summary and Comparative Analysis of Proposals on Arbitration

A. Proposals

12. In order to further improve the GATT dispute settlement system, various proposals have been made to make available to disputing parties an arbitration procedure in addition to the various other possible means of dispute settlement within GATT. One proposal (MTN.GNG/NG13/W/6) has been to provide for arbitration by a neutral body as a formally available technique of GATT dispute settlement for defined classes of cases, or by prior agreement of the disputing parties on an ad hoc basis. The arbitrators' decision would not require approval by the GATT Council or by a GATT Code Committee. But, to safeguard the interests of other contracting parties, it would have to be provided that decisions of such an arbitration process could not bind other contracting parties or prejudice their rights and interests. Arbitration would be available whenever both disputing parties agree, as an alternative to the normal dispute settlement process. In addition, there might be classes of disputes where arbitration should be required in lieu of the normal panel process. If arbitration proves workable and useful, use of the device might subsequently be expanded.

13. Another proposal (MTN.GNG/NG13/W/8) has been that, if a dispute is not settled through consultations or conciliation or if the GATT Council fails to adopt a Panel report submitted to it, a party to the dispute may invoke a previously agreed arbitration clause or agree with the other party on an ad hoc compromissory clause with a view to submitting the dispute to arbitration. The compromis or arbitration clause should be submitted to the Council. The CONTRACTING PARTIES could thus exercise supervision over the subject of the arbitration and over the arbitration procedure adopted by the parties to the dispute, and the Council might reject the arbitration clause on grounds to be defined. The CONTRACTING PARTIES might also agree themselves on an arbitration procedure to be applied by the parties to the

dispute. Issues not settled by such a general GATT arbitration procedure would be settled by the arbitration clause. The CONTRACTING PARTIES would see to the implementation of the arbitral decision, which would be binding and final for the parties to the dispute.

14. Another proposal (MTN.GNG/NG13/W/10) has emphasized that it is the sole responsibility of the CONTRACTING PARTIES to decide on the conformity of a particular measure with the General Agreement and that, in order to ensure coherence of the GATT system, the GATT Council should have a formal rôle in the initiation of the arbitration procedure and in the addressing of the arbitration award.

15. Still another proposal (MTN.GNG/NG13/W/12) said that arbitration on a consensus basis is an option that already exists in the GATT and has been used in the past. This arbitration procedure could be institutionalized. In addition, a Declaration by the CONTRACTING PARTIES to have recourse to this procedure in conflicts of a factual nature could encourage greater use of it. It would be difficult to define a priori the categories of disputes where mandatory arbitration should be prescribed in place of the normal panel procedure. Moreover, it would not be easy to safeguard properly the rights and interests of third parties. The categories of disputes that could be handled by arbitration should be factual and not involve questions of interpretation or of conformity with the General Agreement. The arbitration award could not constitute a legal precedent.

16. It was said (MTN.GNG/NG13/W/13) that the use of mutually agreed arbitration could be facilitated by the roster of GATT panelists. The interests of third GATT contracting parties would need to be protected. One way to ensure this would be to provide a monitoring function for the Council of the outcome of the arbitration so that third parties might more readily ensure that they were not adversely affected. Perhaps the results of the arbitration could be considered to stand unless the Council "disapproved" of them.

17. Another view (MTN.GNG/NG13/W/19) was that, if disputants agreed to resort to arbitration on the basis of mutually agreed terms and conditions as an alternative to panel proceedings, the arbitration clause agreed between the disputants should be referred to and approved by the Council in order to safeguard the interests of third parties. The result of the arbitration should likewise be submitted to the Council. The Council would take note of the report and allow third parties to express their views on the report.

B. Present GATT Rules and GATT Practices

18. Article 93 of the still-born Havana Charter began with a first paragraph that was largely identical with the present GATT Article XXIII:1, and continued with two paragraphs dealing with arbitration in the following terms:

"2. The Members concerned may submit the matter arising under paragraph 1 to arbitration upon terms agreed between them; provided that the decision of the arbitrator shall not be binding for any purpose upon the Organization or upon any Member other than the members participating in the arbitration."

"3. The Members concerned shall inform the Organization generally of the progress and outcome of any discussion, consultation or arbitration undertaken under this Charter."

Additional provisions relating to arbitration were included in Article 94 of the Havana Charter. Paragraph 2 of this Article provided that, whenever a complaint under Article 93, paragraph 1, was referred by any member concerned to the Executive Board:

"The Executive Board shall promptly investigate the matter and shall decide whether any nullification or impairment within the terms of paragraph 1 of Article 93 in fact exists. It shall then take such of the following steps as may be appropriate:

- (a) decide that the matter does not call for any action;
- (b) recommend further consultation to the Members concerned;
- (c) refer the matter to arbitration upon such terms as may be agreed between the Executive Board and the Members concerned;
- (d) in any matter arising under paragraph 1(a) of Article 93, request the Member concerned to take such action as may be necessary for the Member to conform to the provisions of this Charter;
- (e) in any matter arising under sub-paragraph (b) or (c) of paragraph 1 of Article 93, make such recommendations to Members as will best assist the Members concerned and contribute to a satisfactory adjustment."

Article 96 of the Havana Charter also made provision for referring disputes to the International Court of Justice and for requesting advisory opinions by the Court on legal questions arising within the scope of the activities of the then envisaged International Trade Organization. None of these various provisions of the Havana Charter relating to arbitration were incorporated into the General Agreement.

19. It appears that several trade agreements concluded among contracting parties (e.g. under GATT Article XXIV) provide for the possibility of settling their respective trade disputes by means of arbitration. Mutually agreed ad hoc arbitration seems to have been resorted to in GATT practice

only rarely. For instance, in October 1963 the EEC and the USA requested the GATT Council to establish a Panel to render an advisory opinion to the two parties in connexion with their negotiations on poultry. The proposed terms of reference of the Panel were as follows:

"To render an advisory opinion to the two parties concerned in order to determine: 'On the basis of the definition of poultry provided in paragraph 02-02 of the Common Customs Tariff of the European Economic Community, and on the basis of the rules of and practices under the GATT, the value (expressed in United States dollars) to be ascribed, as of 1 September 1960, in the context of the unbindings concerning this product, to United States exports of poultry to the Federal Republic of Germany.'"

On 29 October 1963, the Council appointed a Panel with these terms of reference, and the two disputing parties agreed to accept the Panel finding as binding. The Panel held a number of meetings in November 1963 and presented its report to the two parties. The parties concerned have complied with the Panel's conclusions (see BISD 12S/65).

C. Issues for Clarification of the Present GATT Rules

20. In order to examine the need for additional GATT rules on arbitration, it might be useful to clarify whether, and to what extent, contracting parties agree on the following issues relating to the present GATT rules:

- (a) Do contracting parties agree that the present GATT rules reserve each contracting party the right to conclude an arbitration agreement submitting an existing or a future "GATT dispute" to international arbitration by a bilaterally-established arbitration body?
- (b) Do contracting parties agree that any such arbitration agreement and arbitration award relating to rights and obligations under GATT cannot curtail the rights of third GATT contracting parties under the General Agreement? Since the authoritative interpretation of the General Agreement lies within the sole responsibility of the CONTRACTING PARTIES: Should the Council pronounce on the (in)compatibility of arbitration clauses and arbitration awards with the General Agreement in order to ensure the coherence of the GATT system?
- (c) Do contracting parties agree that GATT Article XXIII:2 already allows two or more GATT contracting parties to request, by common agreement among all parties to the GATT dispute concerned, the CONTRACTING PARTIES (or the Council) to establish a Panel with the mandate of rendering an arbitration award binding on the disputing parties without need for approval of the report by the Council and without prejudice to the rights of third GATT contracting parties (see the precedent of the "chicken panel" referred to above in paragraph 19)? Do contracting parties agree that the present GATT rules do not

provide for a "right to an arbitration panel" and that it remains within the discretion of the GATT CONTRACTING PARTIES (Council) to decide whether a panel requested pursuant to GATT Article XXIII:2 should be established with the traditional terms of reference or, if so requested by all disputant parties, with a mutually agreed "arbitration mandate"?

- (d) Do contracting parties agree that the present GATT rules also preserve the freedom of each contracting party to conclude a general, anticipated arbitration agreement that provides for a unilateral right of each party to such an agreement to request the establishment of an arbitration panel either under GATT Article XXIII:2 by the GATT CONTRACTING PARTIES (with terms of reference to be defined by the CONTRACTING PARTIES in agreement with the disputants) or, if the CONTRACTING PARTIES decide not to grant such a request, outside GATT pursuant to procedures laid down in the arbitration agreement?
- (e) Do contracting parties agree that the requirement under GATT Article X:1 - that judicial decisions affecting imports or exports "shall be published promptly in such a manner as to enable governments and traders to become acquainted with them" - extends also to awards by arbitration bodies established by GATT contracting parties either inside or outside GATT, if the arbitration award decides on the interpretation and application of GATT rules in the contracting parties concerned?
- (f) Is there a need for a formal "understanding" or agreed interpretation by the CONTRACTING PARTIES clarifying the present GATT rules in respect of the availability of arbitration under the current GATT rules? Or would it be wiser to clarify these rules on a case-by-case basis whenever contracting parties actually resort to arbitration and raise the questions in GATT practice?

D. Issues for Consideration of Additional GATT Rules

21. The need for additional GATT rules on arbitration depends on the prevailing views on the availability of arbitration under the current GATT rules. The contracting parties may wish to consider the following issues:

- (a) Is there a need for additional GATT rules recognizing the availability and promoting the use of arbitration among GATT contracting parties?
- (b) Should the CONTRACTING PARTIES formally recognize a right under GATT Article XXIII:2 to request, by common agreement (either an "ad hoc compromis" or an "anticipated compromis") among the disputing contracting parties, the establishment by the CONTRACTING PARTIES of an ad hoc panel with an arbitration mandate agreed among the disputants and accepted by the Council as being compatible with the multilateral GATT legal system?

- (c) Should the GATT CONTRACTING PARTIES encourage recourse to GATT Article XXIII:2 rather than to arbitration outside GATT by recognizing that GATT Article XXIII:2 and the pertinent GATT dispute settlement procedures may be applied, mutatis mutandis, also to arbitration panels established by the GATT Council and that arbitration panels established by the GATT Council may receive the same technical, economic, legal and administrative assistance from the GATT secretariat as other GATT panels established in accordance with the traditional GATT dispute settlement procedure?
- (d) Would the flexibility and acceptability of arbitration be increased by leaving the elaboration of additional arbitration rules (e.g. on arbitration clauses, forms of arbitration, selection of arbitrators, terms of reference, applicable law and procedures, effects of the award) to the initiative of those contracting parties which actually conclude arbitration agreements, subject to the proviso that the terms of reference of arbitration panels established under GATT Article XXIII:2 must be approved by the CONTRACTING PARTIES? Or should the GATT CONTRACTING PARTIES draw up general (mandatory or optional) arbitration rules and procedures?
- (e) Should the CONTRACTING PARTIES introduce a requirement to notify to GATT bilaterally agreed arbitration clauses as well as the initiation and outcome of an arbitration proceeding relating to GATT rights and obligations?
- (f) Should the GATT CONTRACTING PARTIES provide for a general arbitration agreement (protocol, code) enabling each party to such an agreement to unilaterally refer certain classes of GATT disputes to an ad hoc or "permanent" arbitration body (e.g. a unilateral right to request an arbitration panel under GATT Article XXIII:2)? Should such a general arbitration agreement require an additional "implementing compromis" and, if so, should it then limit the freedom of the disputant contracting parties to refuse to set up such an "implementing compromis" (e.g. by enabling the establishment of an "arbitration panel" by the GATT Council at the unilateral request of any party to a general arbitration agreement)? Should such a general arbitration agreement also limit the freedom of the disputant contracting parties to determine the contents of an "implementing compromis" (e.g. the freedom to determine the jurisdiction of the arbitral body, the arbitrators, the applicable rules and procedures)?