ALUMNI ARTICLES

NAPSTER NEAR AND FAR: WILL THE NINTH CIRCUIT'S RULING AFFECT SECONDARY INFRINGEMENT IN THE OUTER REACHES OF CYBERSPACE?

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I. Introduction

In A&M Records, Inc. v. Napster, Inc., the Court of Appeals for the Ninth Circuit in large part, upheld the preliminary injunction against Napster, Inc. ("Napster") based on its finding that Napster is likely to be proven a contributory and vicarious infringer² of the rights of copyright holders in sound recordings

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^{1.} A&M Records, Inc. v. Napster, Inc., 239 F.3d 1004 (9th Cir. 2001) [hereinafter $Napster\ II$].

^{2.} Contributory and vicarious infringement is actionable under the Copyright Act of 1976 which grants the owners of copyrights the exclusive rights "to do and to authorize" the reproduction and distribution of their works. Copyright Act of 1976, 17 U.S.C. § 106 (2000) [hereinafter CA]; Gershwin Publishing Corp. v. Columbia Artists Mgt., Inc., 443 F.2d 1159, 1162 (2d Cir.

and musical compositions.³ In the wake of the Ninth Circuit's decision, new Napster-like file-trading services remain undeterred. The rapid transfer of songs on the Internet is made possible through digital MP3 technology.⁴ Copying or "ripping" audio compact disks directly onto a computer's hard drive in the compressed MP3 format allows users of Napster (and virtually all other music-swapping services on the Internet) to store and rapidly transfer or transmit the copied music from one computer to another.⁵ Yet, even as Napster struggles to gain legal legitimacy,⁶ new applications are surfacing to per-

1971); GB Marketing USA, Inc. v. Gerolsteiner Brunnen GmbH & Co., 782 F. Supp. 763, 772 (W.D.N.Y. 1991).

- 3. As of the date of this writing, members of the House of Representatives are urging the adoption of the Music Online Competition Act, which would amend copyright law to extend the same protection to legitimate online music distributors as exists for radio, cable and satellite broadcasters. H.R. 2724, 107th Cong. (2001). See also Brian Krebs, Key House Leaders Lobby to Defeat Digital Music Bill, Newsbytes (Sept. 20, 2001), at http://www.newsbytes.com/news/01/170343.html.
- 4. MP3 stands for MPEG-3, a standard file format for storage of audio recording in a digital form set by the Moving Picture Experts Group. *See Napster II*, 239 F.3d at 1011. Songs copied in MP3 format are virtually indistinguishable to the human ear from the original recordings. *See* UMG Recordings v. MP3.com, Inc., 92 F. Supp. 2d 349 (S.D.N.Y. 2000); Aaron M. Bailey, *A Nation of Felons?*, 50 Am. U. L. Rev. 473, 479 n.30 (2000).
 - 5. See Napster II, 239 F.3d at 1011.
- 6. See Brad King, Napster's New Tune: Pay Labels, Wired News (Sept. 7, 2001), at http://www.wired.com/news/mp3/0,1285,46636,00.html. Not only has Napster acquired security technology to aid it in operating lawfully, it has licensed that technology to BeMusic, Inc., ("BeMusic") the operator of the record club BMG Music Service, CDNow, an on-line music retailer, and Myplay, Inc., a music locker. See Kevin Featherly, Napster Licenses Security Tech to Bertelsmann's BeMusic, Newsbytes (Oct. 23, 2001), at http://www.newsbytes.com. BeMusic is owned by Bertelsmann AG ("Bertelsmann"), a German company that controls the recording label giant BMG Recorded Music ("BMG"), one of Napster's former legal pursuers. See id.

Indeed, all the major traditional record labels that pursued Napster in front of Chief Judge Marilyn Hall Patel are developing their own legitimate, on-line music services. For instance, Vivendi Universal S.A.'s Universal Music Group, and Sony Corporation's Sony Music Entertainment, Inc., who joined to create the on-line music venture PressPlay, struck deals with six independent record labels to enhance the on-line music selection they will be offering from their own labels as well as from EMI Group Plc.'s EMI labels ("EMI"). See Reuters, PressPlay in Ticense Deals with 6 Record Labels, HINDUSTAN TIMES (Oct. 18, 2001), at http://www.hindustantimes.com. Access to music on PressPlay will be offered through, among others, MP3.com, Inc.

form much the same function. For example, FastTrack, Audiogalaxy, iMesh and Gnutella were used to download 3.05 billion music, movie and software files during the month of August 2001 alone.⁷

("MP3.com"). See id. The other major labels, AOL Time Warner, Inc., Bertesmann and EMI, are backing an on-line music subscription service called MusicNet.com. See Dick Kelsey, Groups Seek Support For Online Music Law, Newsbytes (Oct. 17, 2001) at http://www.newsbytes.com.

Warner Music Group has also announced a licensing deal with Echo Networks, a privately held "stand-alone" on-line music provider based in San Francisco. See Reuters, Warner Music and Echo Networks in Licensing Deal (Nov. 5, 2001), available at http://www.lawtomation.com/news/mp3news/mp3110501.html. Ironically, it appears that the United States Justice Department is conducting an investigation into the major record companies' plans for fear that they may prevent fair competition in the market. See Download Sites Face More Scrutiny, BBC News (Oct. 16, 2001), at http://news.bbc.co.uk. Members of the European Union have expressed similar concerns at a conference in Brussels in October 2001. See EU 'Threat' Over Download Sites, BBC News (Oct. 15, 2001), at http://news.bbc.co.uk.

On February 22, 2002, Chief Judge Patel ruled that not only do the record companies have to prove that they own the music at issue, they must also show that the copyrights were not used to monopolize the distribution of digital music. See Brad King, Judge: If You Own Music, Prove It, WIRED NEWS (Feb. 22, 2002), at http://www.wired.com [hereinafter If You Own Music]. The record companies have three weeks to comply with Chief Judge Patel's order. Id. A hearing on the anti-competitive allegations against the record companies has been set for March 27, 2002. See John Borland, Napster Court Win Puts Labels in Spotlight, CNET NEWS.COM (Feb. 22, 2002), at http://www.news.com [hereinafter Napster Court Win]. This ruling does not affect either Chief Judge Patel's or the Ninth Circuit's analysis of Napster's own culpable behavior. Rather, if plaintiffs cannot prove that they own the copyrights at issue, they will have failed to prove a prima facie case of direct infringement of their copyrights. There is no doubt, however, that someone's copyrights have been infringed.

7. Napster Eclipsed by Newcomers, Wired News (Sept. 6, 2001), at http://www.wired.com. See also Reuters, Music Downloading Rises in August, *Topping* Napster (Sept. 6, 2001), availablehttp://www.siliconvalley.com/docs/news/reutrs_wire/14650381.htm; John Borland, Rocky Financial Road Awaits File Swappers, CNET News.com (Sept. 21, 2001), at http://news.cnet.com/news/0-1005-200-7230930.html ("Already, millions of people have migrated to start-ups such as [MusicCity.com, Inc. ("MusicCity")], Audiogalaxy and Aimster.") [hereinafter Rocky Road]; Jason Hoppin, 9th Circuit Is Sick of Hearing Napster Tune, RECORDER (Sept. 20, 2001), at http://www.law.com (noting that on September 18, 2001, seven of the top eleven downloaded programs available at CNET Download.com, http://download.cnet.com, enabled file-sharing and were available for downloading at no charge).

The fact that file-trading services are burgeoning implies that the *Napster* decision will serve as an important precedent in copyright infringement cases set in cyberspace.⁸ Coupled with the truly global scope of the Internet, the question of how *Napster* will impact copyright cases against infringers in this country, but particularly abroad, is ripe for examination.⁹

The Ninth Circuit in *Napster* held that "if a computer system operator learns of specific infringing material available on his system and fails to purge such material from the system, the operator knows of and contributes to direct infringement." Further, the court found that Napster "provides 'the site and facilities' for direct infringement," and that it therefore "materially contributed to the direct infringement."

Read broadly, *Napster* provides precedent for courts to hold all service providers, including foreign providers, who have

Most recently, *Wired.com* reported a Webnoise study which predicted that FastTrack would surpass Napster's volume and use by the end of November 2001. *See* Brad King, *EMI Has No Fears of Peers*, WIRED NEWS (Nov. 6, 2001), *at* http://wired.com/news/mp3/0,1285,48147,00.html [hereinafter *EMI Has No Fears*]. The same article reported a business arrangement in a related industry, the distribution of on-line videos, between strange bedfellows – EMI, Jive Media Technology and Gnutella software developer Live Wire – that has made it possible for viewers to search and download videos off the Internet. *See id*.

- 8. Indeed the Recording Industry Association of America ("RIAA") and the Motion Picture Association of America ("MPAA") have initiated litigation against newer peer-to-peer services, MusicCity, Kazaa and Grokster, Ltd. ("Grokster") for secondary copyright infringement liability. See Metro-Goldwyn-Mayer, Inc. v. Grokster, Ltd., No. 01-8541 (C.D. Cal. filed Oct. 2, 2001) (against Grokster, MusicCity, MusicCity Networks, Inc. and Consumer Empowerment BV); John Paczkowski, Good Morning Silicon Valley, SILICON VALLEY.COM (Mar. 14, 2001), at http://www.siliconvalley.com/docs/opinion/gmsv/archive01/morn10032001.htm (reporting that the RIAA and MPAA were contemplating filing law suits).
- 9. Indeed, among the multitude of discussions exploring this timely subject, the Bureau of Nation Affairs' Third Annual Public Policy Forum on International E-Commerce & Internet Regulation, hosted in part by Pike & Fisher, Inc., on November 14, 2001, was devoted to the topic of what legal challenges businesses face in operating on the Internet. Letter from U. Joseph Hecker, President, Pike & Fisher, Inc., to Colleagues Attending the Third Annual Forum (Nov. 14, 2001) (on file with Journal). The discussion focused on international jurisdiction and cross-border infringement and piracy." *Id.*
 - 10. Napster II, 239 F.3d at 1021.
- 11. *Id.* at 1022 (citing Fonovisa, Inc. v. Cherry Auction, Inc., 76 F.3d 259, 264 (9th Cir. 1996).

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reason to know that their software or website is being used for infringing purposes, liable to copyright holders for contributory infringement.¹² But will the *Napster* holding reach foreign contributory infringers? In holding Napster liable, did the Ninth Circuit provide the perfect precedent for holding a foreign company whose software is available on the Internet liable to a United States copyright holder for contributory infringement?

This Article will first study the *Napster* decision, concentrating in Section II on the Ninth Circuit's factual findings and its contributory infringement analysis. Then, in Section III, with the aid of a hypothetical in which a contributory infringement case is brought in a U.S. federal court by a U.S. copyright holder against a foreign Napster-like service provider, this Article will attempt to discern the likely outcome of such a dispute. The hypothetical will focus on the likely jurisdictional analysis a court would undertake, in the context of cyberspace, to determine whether a foreign defendant may indeed be held liable in a foreign forum for an act that may (or may not) be permitted under the defendant's sovereign's jurisprudence.¹³

^{12.} The tort of contributory infringement is well developed in American jurisprudence. This is not so in other countries, such as Canada, where a cause of action for contributory infringement does not lie. See MICHAEL A. GEIST, INTERNET LAW IN CANADA 472-525 (2d ed. 2000) (no contributory infringement under Canadian law). Other differences, for example, include Europe, where copyright owners enjoy "moral rights" in their works. See, e.g., Pamela Samuelson, Privacy As Intellectual Property?, 52 STAN. L. REV. 1125, 1146 (2000).

^{13.} Consideration of this topic will inevitably spur the pragmatic question of whether, having cleared the pertinent procedural and substantive hurdles, a U.S. judgment would be enforced abroad. This is especially true in light of the well-acknowledged dearth of international treaties on the issue of enforcement of judgments – particularly in the context of intellectual property disputes in cyberspace. For example, the disparateness of Internet "Ecommerce" law, which broadly covers companies like Napster, is evidenced by the inability of the Convention on Jurisdiction and Foreign Judgments in Civil and Commercial Matters ("Convention on Jurisdiction") to arrive at a treaty which facilitates the enforcement of civil judgments across borders. Andy Sullivan, Global E-Commerce Treaty Hits Snag, INFO-SEC.COM (Feb. 2, 2001), at http://www.info-sec.com/commerce/01/commerce_022101a_j.shtml. See also Proposed Convention on Jurisdiction and Foreign Judgments in Civil Commercial Matters, athttp://www.cptech.org/ecom/ jurisdiction/hague.html (last visited Mar. 10, 2002). Formed in 1996, the Convention on Jurisdiction "has been hung up since 1999 over a disagreement over how business-consumer disputes should be settled." See Sullivan, supra note 13.

The hypothetical will also show that the liability analysis courts must undertake to determine whether one may be adjudged a contributory infringer complements the jurisdictional analysis such that, in most cases, the finding of jurisdiction will lead directly to a finding of liability. Finally, given the factual predicate under which *Napster* was decided, Section IV concludes that Napster-like services, no-matter where they are based, must beware.

II. A&M RECORDS, INC. V. NAPSTER, INC.

Until it was enjoined from operating, Napster was a popular music-sharing program created by a college student named Shawn Fanning as a favor to a friend who wanted to find obscure rap music on the Internet.¹⁴ The Napster program Fanning created collected the names of the MP3 files on all of its

Though copyright issues are not necessarily inherent in ecommerce, the stumbling blocks to achieving a comprehensive treaty on the enforcement of judgments share many of the same characteristics with copyright law. By way of example, the key area of disagreement appears to be over jurisdictional issues, i.e., the current draft of the Convention on Jurisdiction makes it unnecessary for aggrieved consumers to file suit outside of their own home countries. Id. This important topic is beyond the scope of this Article. For an interesting criticism of the standards currently in place and the initiatives that have developed and stalled, see Rochelle Cooper Dreyfuss, An Alert to the Intellectual Property Bar: The Hague Judgments Convention, 2001 U. ILL. L. Rev. 421 (2001) (discussing the Berne Convention for the Protection of Literary and Artistic Works ("Berne Convention"), the Paris Convention for the Protection of Industrial Property, the Agreement on Trade-Related Aspects of Intellectual Property Rights ("TRIPS") and proposed Hague Conference on Private International Law Convention on Jurisdiction and the Recognition of Foreign Judgments). See also Graeme B. Dinwoodie, A New Copyright Order: Why National Courts Should Create Global Norms, 149 U. PA. L. REV. 469 (2000) (exploring, among other topics, provisions of Berne Convention, the World Intellectual Property Organization ("WIPO") and TRIPS); Michael J. O'Sullivan, International Copyright: Protection for Copyright Holders in the Internet Age, 13 N.Y. INT'L L. REV. 1 (2000) (discussing WIPO, the Berne Convention, TRIPS, the WIPO Copyright Treaty and the WIPO Performances and Phonograms Treaty). TRIPS requires member countries of the World Trade Organization to comport their copyright laws with the substantive provisions of the Berne Convention. See Neil Weinstock Netanel. From the Dead Sea Scrolls to the Digital Millennium: Recent Developments in Copyright Law, 9 Tex. Intell. Prop. L.J. 19, 61 (2000).

14. See Sarah D. Glasebrook, Comment, "Sharing's Only Fun When It's Not Your Stuff": Napster.com Pushes the Envelope of Indirect Copyright Infringement, 69 UMKC L. REV. 811, 811-12 (2001).

users' computers in a searchable index, so that users could ascertain the songs available for copying through Napster and select the songs they wished to download onto their own computers from that list.¹⁵ The actual transfers of files took place between users so that no copies were made or retained on Napster's servers.¹⁶ Undoubtedly recognizing that Napster would not be found liable for direct copyright infringement because it did not itself engage in the copying of their copyrighted music,¹⁷ under the auspices of the Recording Industry Association of America ("RIAA"), eighteen major record companies filed a complaint against Napster for contributory and vicarious infringement.¹⁸

On July 26, 2000, having found that plaintiffs had established a likelihood of success on their contributory and vicarious infringement claims against Napster, 19 Chief Judge Marilyn Patel of the District Court for the Northern District of California issued a preliminary injunction enjoining Napster "from engaging in, or facilitating others in copying, downloading, uploading, transmitting, or distributing plaintiffs' copyrighted musical compositions and sound recordings, protected by either federal or state law, without express permission of the rights owner."20 Seven months later, having accepted jurisdiction to review Chief Judge Patel's interlocutory order,²¹ the Ninth Circuit in part vacated the preliminary injunction but let stand most of Chief Judge Patel's conclusions of law regarding Napster's likely liability.²² The Ninth Circuit's analysis of Napster's liability for the peer-to-peer file sharing it facilitated defines the boundaries of secondary infringement 1-

^{15.} *Id*.

^{16.} *Id*.

^{17.} See Jane C. Ginsburg, Copyright Use and Excuse on the Internet, 24 COLUM. V-LA J.L. & ARTS 1, 28 (2000) ("[T]here is no basis for a primary infringement claim against Napster. Napster does not store files on its servers. Nor does Napster itself effect the distribution of copies").

^{18.} See A&M Records, Inc. v. Napster, 114 F. Supp. 2d 896, 900 (N.D. Cal. 2000) [hereinafter Napster I].

^{19.} *Id.* at 925.

^{20.} *Id.* at 927. This written opinion, slightly modifying the injunction, was issued on August 10, 2000.

^{21.} The Ninth Circuit heard the appeal pursuant to 28 U.S.C. § 1292(a)(1) (1994). See Napster II, 239 F.3d 1004, 1011 (9th Cir. 2001).

^{22.} See generally Napster II, 239 F.3d at 1004.

ability vis-à- vis the Internet in the United States. When other Internet music providers such as Napster are hauled into court here, this is the case to which plaintiffs will cite.

The Ninth Circuit, reviewing Chief Judge Patel's ruling for a possible abuse of discretion, found that through its MusicShare software:

Napster allowed its users to: (1) make MP3 music files stored on individual computer hard drives available for copying by other Napster users; (2) search for MP3 music files stored on other users' computers; and (3) transfer exact copies of the contents of other users' MP3 files from one computer to another via the Internet.²³

Napster was able to provide this service in part through the creation of a "search index," maintained on Napster's servers, which allowed users to access a collective directory of all the names of the songs Napster users stored on their own individual computers.²⁴ Provided the host (the user whose songs another user wanted to access) was logged on at the same time as the requesting user, Napster's software provided the means by which music could be transferred from one hard drive to another, or "peer-to-peer."²⁵

In order to prove their case for a preliminary injunction, plaintiffs first had to present a prima facie case that the peers were themselves engaging in direct infringement. Therefore, plaintiffs had to and did demonstrate that they both owned the works at issue and that at least one exclusive right granted to copyright holders under 17 U.S.C. § 106²⁶ was violated.²⁷ It is

^{23.} Id. at 1011.

^{24.} See id. at 1012.

^{25.} Id.

^{26.} Section 106 grants six exclusive rights to owners of copyrights, including the right to reproduce and distribute their works. See CA, 17 U.S.C. §106 (1)-(6) (2000). Here the court found the plaintiffs' exclusive rights to reproduction and distribution were violated. Napster II, 239 F.3d at 1014 ("Napster users who upload file names to the search index for others to copy violate plaintiffs' distribution rights. Napster users who download files containing copyrighted music violate plaintiff's reproduction rights."). In what one reporter called "a stunning turnaround," the record companies' ownership of the copyrights at issue has now been called into question. If You Own Music, supra note 6. Chief Judge Patel ruled on February 22, 2002 that plaintiffs were obliged to prove their ownership of the copyrights infringed. In re Napster, Inc. Copyright Litigation, No. 00-1369 (N.D. Cal. Feb. 22, 2002) (order

important to note that the rights under which plaintiffs sued are derived from the Copyright Act of 1976 ("Copyright Act").²⁸ Had the copyrights been foreign, the analysis of the Ninth Circuit would have been much more complicated and exhaustive.²⁹ Having found that plaintiffs established the direct infringement, the Ninth Circuit went on to review Chief Judge Patel's ruling that plaintiffs established their right to a preliminary injunction by demonstrating that Napster was a contributory infringer.³⁰

A. Contributory Infringement

In order to establish that Napster would likely be found liable for contributory infringement, plaintiffs had to establish that Napster knew or had reason to know of its users' infringing activities, and that Napster materially contributed to its users' infringing activity.³¹ The Ninth Circuit agreed with the district court that "Napster had both actual and constructive

granting defendant's motion for additional discovery), available at http://www.cand.uscourts.gov. See also Napster Court Win, supra note 6.

- 27. Napster II, 239 F.3d at 1013. In finding that direct infringement was indeed taking place, the court examined Napster's affirmative defense of "fair use." Id. at 1014. 17 U.S.C. § 107 provides that fair use of a copyrighted work is not infringement. Section 107 also sets out factors to help courts determine whether defendant's activities constitute fair use:
 - (1) [T]he purpose and character of the use; (2) the nature of the copyrighted work; (3) the amount and substantiality of the portion of the work used in relation to the copyrighted work as a whole; and (4) the effect of the use on the potential markets [for the work or on the work's value].
- CA, 17 U.S.C. § 107. The Ninth Circuit rejected Napster's arguments on these traditional fair use factors, and went on to uphold Chief Judge Patel's rejection of Napster's novel argument that its users' copying of plaintiffs works was not infringement because they downloaded the works to sample them to decide whether to buy the albums. See Napster II, 239 F.3d at 1018. The Ninth Circuit also upheld Chief Judge Patel's finding that "space-shifting," the downloading of music already owned by the user, is not fair use. See id. at 1019. The fair use doctrine will undoubtedly be applied in many creative new ways in attempts to thwart liability. This topic is deserving of its own plenary treatment and will not be explored further here.
 - 28. CA, 17 U.S.C. §§ 101-1332 (2000).
 - 29. See infra note 59 (discussing choice of law issues).
 - 30. Napster II, 239 F.3d at 1019-23.
 - 31. Id. at 1019-20.

knowledge of direct infringement."32 However, the court of appeals appears to have differed with Chief Judge Patel's conclusion that Napster need not have known of "specific acts of infringement" to satisfy this prong. 33 Citing Religious Technology Center v. Netcom On-Line Communication Services, Inc.,34 the Ninth Circuit held that "absent any specific information which identified infringing activity, a computer system operator cannot be liable for contributory infringement merely because the structure of the system allows for the exchange of copyrighted material."35 Perhaps inconsistently, in rejecting Napster's argument that it was saved from liability under the Sony doctrine,³⁶ the Ninth Circuit found that "[r]egardless of the number of Napster's infringing versus noninfringing uses, the evidentiary record here supported the district court's finding that plaintiffs would likely prevail in establishing that Napster knew or had reason to know of its users' infringement of plain-

^{32.} Id. at 1020.

^{33.} Chief Judge Patel held that "[t]he law does not require actual knowledge of specific acts of infringement." *Napster I*, 114 F. Supp. 2d 896, 918 (N.D. Cal. 2000).

^{34.} Religious Tech. Ctr. v. Netcom On-Line Communication Services, Inc., 907 F. Supp. 1361 (N.D. Cal. 1985).

^{35.} Napster II, 239 F.3d at 1021.

^{36.} In Sony Corporation of America v. Universal City Studios, Inc., the Supreme Court refused to impute knowledge of infringing activities to defendants where defendants' products were capable of "substantial noninfringing uses." 464 U.S. 417, 442 (1984) (articulating the "Betamax" standard for contributory infringement). Rather, the Sony Court required proof that defendants in fact had knowledge, either constructive or actual. Id. This decision carves out an exception from liability in cases where a "staple Article of commerce" is capable of substantial non-infringing activity. Id. The Betamax defense may be used by MusicCity, Grokster and Kazaa to defend against the RIAA and the MPAA in their recently filed suit for infringement against the peer-to-peers. See Metro-Goldwyn-Mayer, Inc. v. Grokster Ltd., No. 01-8541 (C.D. Cal. filed Oct. 2, 2001); John Borland, File-Swapping Case May Break New Ground, CNET NEWS.COM (Nov. 6, 2001), at http://news/cnet.com/ news/01005-200-7798704.html (stating that the Electronic Frontier Foundation, which will represent the defendants, will likely argue that the allegedly infringing software, which helps users develop file-sharing networks on their own, is capable of non-infringing uses, and that, because defendants have no control over how their software is used, they are analogous to the video cassette recorder ("VCR") distributors who were let off the hook by the Supreme Court in *Sony*).

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tiffs' copyrights."³⁷ In this way, the Ninth Circuit indirectly addressed the district court's observation that the "Betamax" standard³⁸ was inapplicable because unlike in *Sony*, where the manufacturer of the VCRs had no control over the product once it was in the marketplace, Napster continued to exercise ongoing control over its service.³⁹

Significantly, however, the Ninth Circuit cautioned that it would "not impute the requisite level of knowledge to Napster merely because peer-to-peer file sharing technology may be used to infringe plaintiffs' copyrights [Contributory infringement will not be found] merely because the structure of the system allows for the exchange of copyrighted material."⁴⁰ Therefore, the appellate court placed heavy emphasis on ætual, rather than constructive, knowledge.⁴¹

As for the second prong of the test, the district court, following Fonovisa, Inc. v. Cherry Auction, Inc.⁴² found that "Napster, Inc. supplies the proprietary software, search engine, servers, and means of establishing a connection between users' computers. Without the support services defendant provides, Napster users could not find and download the music they want with the ease of which defendant boasts."⁴³ The Ninth Circuit agreed with the district court that Napster "materially contributed" to the infringing activity by providing "the site and facilities' for direct infringement."⁴⁴

^{37.} Napster II, 239 F.3d at 1021 (requiring that a defendant be notified of "specific acts of infringement," seems to remove the having "reason to know" possibility from the inquiry).

^{38.} See Sony, 464 U.S. at 442.

^{39.} Napster I, 114 F. Supp. 2d 896, 916 (N.D. Cal. 2000).

^{40.} Napster II, 239 F.3d at 1020-21.

^{41.} This holding is in line with the Digital Millennium Copyright Act of 1998 ("DMCA"), Pub. L. No. 105-304, 112 Stat. 2860 (codified as amended at 17 U.S.C. § 10 and scattered sections), which codified the requirement of knowledge or "volition" for liability for contributory infringement. See Bailey, supra note 4, at 502-03 (noting that the DMCA essentially codifies the holding in Religious Tech. Ctr. v. Netcom Online Communications Services, Inc., 907 F. Supp. 1361, 1373-74 (N.D. Cal. 1995), namely, that an Internet service provider ("ISP") could not be liable for contributory infringement where it had no knowledge, nor could it know that infringing material was posted on its system). The DMCA is Congress' attempt to conform U.S. copyright law to WIPO treaties.

^{42.} Fonovisa, Inc. v. Cherry Auction, Inc., 76 F.3d 259 (9th Cir. 1996).

^{43.} Napster I, 114 F. Supp. 2d at 920.

^{44.} Napster II, 239 F.3d at 1022.

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B. Vicarious Infringement⁴⁵

Vicarious infringement liability, an outgrowth of the respondeat superior doctrine, "extends beyond an employer/employee relationship" to situations in which the defendant "has the right and ability to supervise the infringing activity and also has a direct financial interest in such activities."46 The Ninth Circuit upheld Chief Judge Patel's finding that, as to economic interest in the direct infringing activity, "[a]mple evidence supports the district court's finding that Napster's future revenue is directly dependent upon 'increases in userbase."47 It also upheld the district court's conclusion as to the supervision prong of the test, but with a caveat. "The ability to block infringers' access to a particular environment for any reason whatsoever is evidence of the right and ability to supervise."48 The district court found that Napster may be liable for vicarious infringement because Napster expressly reserved its rights to refuse service or terminate accounts for any reason, but failed to police its service.⁴⁹ According to the Ninth Circuit, however, the lower court "failed to recognize that the bound aries of the premises that Napster 'controls and patrols' are limited" by its architecture. 50 Nonetheless, that the search indexes were "within the 'premises' that Napster has the ability to police," combined with Napster's financial benefit from the infringing activity, was enough to lead to the imposition of vicarious liability.⁵¹

^{45.} The Ninth Circuit's vicarious liability analysis is not discussed in this Article in great detail. As the brief discussion that follows demonstrates, both the district court and the appellate court placed much emphasis on Napster's express reservation of rights to police its site. As a practical matter, the *Napster* decisions broadcast a way in which future defendants may escape vicarious liability by structuring their systems such that they are unable to police their sites. In any event, the Ninth Circuit's upholding of the district court's findings as to vicarious liability appears to have been half-hearted.

^{46.} Napster II, 239 F.3d at 1022 (quoting Fonovisa, 76 F.3d at 262).

^{47.} Id. at 1023.

^{48.} Id.

^{49.} Napster I, 114 F. Supp. 2d at 921.

^{50.} Napster II, 239 F.3d at 1023-24.

^{51.} *Id.* at 1024.

After addressing Napster's remaining arguments in its defense,⁵² the Ninth Circuit proceeded to direct the district court to modify the injunction against Napster to place the burden on plaintiffs to inform Napster of the availability of their copyrighted works on the Napster system.⁵³ Subsequently, on March 5, 2001, Chief Judge Patel modified the injunction against Napster.⁵⁴ Not surprisingly, the modified injunction has been challenged by both sides, each arguing Chief Judge Patel's decision regarding the injunction did not go far enough. The Ninth Circuit has yet to rule on this issue.⁵⁵ It may become moot, however, with Chief Judge Patel's decision on the RIAA's motion for summary judgment, argued in October 2001.⁵⁶

- 53. Napster II, 239 F.3d at 1027.
- $54.\ See$ A&M Records, Inc. v. Napster, Inc., No. C 99-5183 MHP, C 00-1369 MHP, 2001 WL 227083 (N.D. Cal. Mar. 5, 2001).
- 55. A&M Records, Inc. v. Napster, Inc., No. 01-15998 (9th Cir. Dec. 10, 2001). See also Appeals Court Hears Arguments in Napster Case, SILICON VALLEY.COM (Dec. 10, 2001), at http://www.siliconvalley.com.
- 56. As of the date of this writing, no decision has been issued. Rather, as discussed in note 6, supra, the case has taken an interesting turn of events, with the record companies suddenly on the defensive. See also Reuters, Napster, Labels Head Back to Court Wednesday, Silicon Valley.com (Oct. 7, 2001), available at http://www.siliconvalley.com/docs/news/reuters_wir/15489851.htm; Reuters, Napster, Music Industry Return to Court, CNET News.com (Oct. 8, 2001), available at http://news/cnet.com/news/0-1005-200-7445627.html. Helping to make the case go away is Dr. Dre and Metallica's summer settlement with Napster. See Jason Hoppin, 9th Circuit Is Sick of Hearing Napster Tune, Recorder (Sept. 20, 2001), available at http://www.law.com. Napster has also settled with music publishers and songwriters for \$26,000,000, plus portions of future profits. See Napster Settles with Music Publishers, Wall St. J., Sep. 25, 2001, at B4.

^{52.} Having earlier disposed of Napster's fair use defenses, see *supra*, note 27, it went on to address its remaining defenses and rejected each one. *Id.* at 1026-27. As to Napster's claim that the Audio Home Recording Act of 1992 ("AHRA"), 17 U.S.C. §§ 1001-1010 (2000), protects its activities, the Ninth Circuit concluded that the AHRA "does not cover the downloading of MP3 files to computer hard drives" because computers are not digital audio recording devices and do not make digital music recordings. *Napster II*, 239 F.3d at 1024. The Ninth Circuit also rejected Napster's waiver, implied license and misuse defenses. *See id.* at 1026. It left for further development at trial the possibility that the DMCA might provide a safe harbor from liability. *See id.* at 1025.

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III. HYPOTHETICAL

Suppose that a Napster-like file-sharing service is launched by a French company named Robin des Bois, S.A. ("Robin des Bois"). The instructions on its website are written in French, but, because it wishes to succeed against its competitors and to ensure a wider user base, it also features instructions in English, the language spoken most throughout the Western world.⁵⁷ As part of its service, Robin des Bois, like Napster, requires its users to register with the company and keeps a central index of all the songs its users have stored on their individual hard drives. Robin des Bois' central index reflects music from around the world, including the ever popular American music that is copyrighted under the United States Copyright Act⁵⁸ and owned by American recording labels, among them, RIAA member A&M Records, Inc. ("A&M"). Unlike Napster, Robin des Bois does not reserve the right to police its site, although it is capable of blocking access to its site by its users. All of Robin des Bois' other features, and the way its system functions, are not materially different from that of Napster. Most importantly, like its namesake, Robin des

^{57.} Another compelling reason for Robin des Bois to put English on its website is that it will be filling Napster's shoes while it remains in litigation. Jupiter Media Metrix has recently reported that the level of Internet file-sharing activity in Europe has dropped by 50% since February 2001. In part, this drop may be attributed to the fact that the majority of European users of file-sharing sites were using Napster, which has been disabled since July 2001. See Bernhard Warner, Study: Online Song-Swapping on Decline in Europe, SILICON VALLEY.COM (Oct. 29, 2001), at http://www.siliconvalley.com/docs/news/reuters_wire/16089871.htm.

On the other hand, the European on-line music market may soon experience a rise in file-sharing activity. Vitaminic, Europe's largest on-line distributor delivering files in the MP3 format, has recently signed a licensing deal with Napster that will give it access to thousands of independent artists. See EMI Has No Fears, supra note 7. While Vitaminic is a legitimate subscription service, the increased awareness and availability of popular music on the Internet in Europe may spark the flourishing of illegitimate music pirates. See Gwendolyn Mariano, Napster Rivals Winning Popularity Contest, CNET News.com (Nov. 5, 2001), at http://news.cnet.com/news/0-1005-200-7788007.html (expanded range of content and interest in file sharing on the rise worldwide). In the United States, no decline has followed Napster's temporary demise. File-sharing activity has jumped by 480% since June 2001. See id. (Webnoise study reports number of music files download using Kazaa, MusicCity and Grokster up 20%).

^{58.} CA, 17 U.S.C. §106 (2000).

Bois has no intention of charging for its service, and no intention of paying for the music available through it. In short, Robin des Bois is not authorized by A&M to distribute its repertoire.

Now suppose A&M, cognizant of the *Napster* decision, contacts Robin des Bois and informs it that A&M's music is indexed on its website, and demands that it "cease and desist" from offering A&M's copyrighted works for distribution. After some time, having heard no response from the French company, A&M brings suit against Robin des Bois in the United States District Court for the Northern District of California, where the court is well versed in the file-sharing phenomenon, and Napster is controlling precedent.⁵⁹ A&M charges that its copyrighted music is being copied and distributed via Robin des Bois' peer-to-peer file-sharing service within the United States and abroad, and accuses Robin des Bois of contributory infringement, seeking a preliminary and permanent injunction against the company. Robin des Bois, in turn, responds to the allegation by bringing a motion to dismiss the complaint based on lack of subject matter and personal jurisdiction,60 and in the alternative, for failure to state a claim.61

^{59.} This hypothetical assumes that the copyrighted works at issue are properly registered with the United States Copyright Office, thereby obviating a lengthy choice of law analysis. Had the copyright at issue been foreign, our district court would likely be obliged to proceed with determining which country's laws should apply to the dispute. See William F. Patry, Choice of Law and International Copyright, 48 Am. J. Comp. L. 383, 385 (2000) (discussing choice of law issues and, in addition, concluding that no choice of law issues will exist where an unauthorized copy of a work is placed on a website outside of the U.S., even when subsequent infringing copying occurs in the U.S. because no cause of action will lie). For a case demonstrating the choice of law problems inherent in international copyright disputes, see National Football League v. TVRadioNow Corp., 53 U.S.P.Q. 2d 1831, 1834 (W.D. Pa. 2000) (dispute regarding whether U.S. or Canadian law governed copyright infringement case where defendant claimed that redistribution of U.S. programming in Canada was not unlawful in Canada, but where the activity would be unlawful in the U.S.). See also Bridgeman Art Library, Ltd. v. Corel Corp., 25 F. Supp. 2d 421, 425 (S.D.N.Y. 1998); Jane C. Ginsburg, Copyright Use and Excuse on the Internet, 24 COLUM.-VLA J.L. & ARTS 1, 41-44 (analyzing TVRadioNow).

^{60.} See FED. R. CIV. P. 12(b)(1)-(2) (motions to dismiss for subject matter jurisdiction and personal jurisdiction, respectively).

^{61.} See Fed. R. Civ. P. 12(b)(6).

A. Subject Matter Jurisdiction or the Extraterritorial Reach of the Copyright Act

It is appropriate to acknowledge that, although the Internet is still a fairly new technology, the answers to most questions borne out of its novelty lie in traditional, well-developed and much tested principles of law.⁶² To begin the analysis, then, one must determine whether a U.S. district court may exercise jurisdiction over a foreign defendant accused of being a con-

62. This sentiment is common throughout the diverse spectrum of the legal community. To wit, Judge Jed Rakoff of the District Court for the Southern District of New York boldly began one of his first opinions in *UMG Recordings v. MP3.com, Inc.*, a copyright infringement case initiated by the RIAA against now-infamous MP3.com, with the following: "The complex marvels of cyberspatial communication may create difficult legal issues; but not in this case. Defendant's infringement of plaintiffs' copyrights is clear." UMG Recordings v. MP3.com, Inc., 92 F. Supp. 2d 349, 350 (S.D.N.Y. 2000). Similarly, the California Court of Appeals, Sixth District, recently wrote that "as a mode of communication and a system of information delivery [the Internet] is new, but the rules governing the protection of property rights, and how that protection may be enforced under the new technology, need not be." Pavlovich v. Superior Court, 109 Cal. Rptr. 2d 909, 912-13 (Cal. Ct. App. 2001).

This sentiment was echoed in academia by Joseph H. Sommer, Counsel for the Federal Reserve Bank of New York, in the *Berkeley Technology Law Journal*: "[C]yberspace is just another battleground for some very old wars." Joseph H. Sommer, *Against Cyberlaw*, 15 Berkeley Tech. L.J. 1145, 1149 (2000). Sommer expounded on his proposition later when he observed that "copyright has always been mediated through the First Amendment and the needs of the copyright industries. We do not have a 'law of the printing press,' or a 'law of the player piano." *Id.* at 1155 (citing White-Smith Music Publ'g Co. v. Apollo Co., 209 U.S. 1 (1908).

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tributory infringer via the Internet.⁶³ This calls for an examination of the extraterritorial reach of the Copyright Act.⁶⁴

It is generally accepted that under 28 U.S.C. § 1338,65 district courts of the United States do not have subject matter ju-

63. The Internet, unlike most applications, defies national boundaries. For example, messages among computers are often transmitted through "packet switching' communication protocols," which allow individual messages to be split up and sent along independent routes (via phone lines or fiber-optic cables or satellites) to a single destination in which the message is reassembled. See Dennis T. Rice, 2001: A Cyberspace Odyssey Through U.S. and E.U. Internet Jurisdiction Over E-Commerce, in FIFTH ANNUAL INTERNET LAW INSTITUTE 421, 445-46 (PLI Intell. Prop. Course, Handbook Series No. G-661, 2001). Websites may be interconnected by way of "hyperlinks," regardless of the locations of their servers. See id. And, especially in the realm of copyrighted music, users simply do not care whether they are downloading from the United States or Germany – or whether they are uploading to Tibet or Bali.

64. See CA, 17 U.S.C § 106 (2000). Strictly speaking, there is a distinction between an analysis of the extraterritorial reach of a statute and subject matter jurisdiction. To obtain subject matter jurisdiction, ordinarily one must show that he is proceeding either under diversity jurisdiction or is seeking adjudication of a federal question. Litigation under the Copyright Act presents a federal question. The right to copyright protection is derived from none other than the United States Constitution. U.S. Const. art. I, § 8, cl. 8. The Copyright Act, being an act of Congress, is a federal statute. Therefore, federal courts clearly have subject matter jurisdiction to hear a copyright infringement claim. However, the scope of the Copyright Act will dictate whether a claim may be brought under it. If a claim is outside the scope of the statute, a litigant cannot avail himself of the statute's prescriptions and a court will be unable to render a decision pursuant to that statute. Courts sometimes refer to this analysis of the extraterritorial reach of the Copyright Act as the analysis of subject matter jurisdiction. For the purposes of this Article, the two concepts will be used interchangeably.

65. Section 1338 states:

- (a) The district courts shall have original jurisdiction of any civil action arising under any Act of Congress relating to patents, plant variety protection, copyrights and trade-marks. Such jurisdiction shall be exclusive of the courts of the states in patent, plant variety protection and copyright cases.
- (b) The district courts shall have original jurisdiction of any civil action asserting a claim of unfair competition when joined with a substantial and related claim under the copyright, patent, plant variety protection or trademark laws.
- (c) Subsections (a) and (b) apply to exclusive rights in mask works under chapter 9 of title 17, and to exclusive rights in designs under chapter 3 of title 17, to the same extent as such subsections apply to copyrights.

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risdiction over actions for infringement of U.S. copyright occurring outside the United States.⁶⁶ On the other hand, American courts have taken jurisdiction over claims where the conduct complained of was foreign but was clearly intended to, and did, have an effect in the United States.⁶⁷ Importantly, in those cases, the courts exercised subject matter jurisdiction over acts

28 U.S.C. § 1338 (2000).

66. See Quantitative Fin. Software, Ltd. v. Infinity Fin. Tech. Inc., 47 U.S.P.Q. 2d 1764, 1765 (S.D.N.Y. 1998). An exception to this rule, "when the type of infringement permits further reproduction abroad – such as the unauthorized manufacture of copyrighted material in the United States . . . the act taking place in the United States at the very least must tself violate the Copyright Act." Id. at 1765. See also Los Angeles News Serv. v. Reuters Television Int'l, Ltd., 149 F.3d 987 (9th Cir. 1998) (permitting recovery against defendant who first copied and transmitted unauthorized work in the U.S. and then transmitted it abroad); Allarcom Pay Television, Ltd. v. Gen. Instrument Corp., 69 F.3d 381, 387 (9th Cir. 1995); Netanel, supra note 13, at 58

Therefore, where an Israeli plaintiff sued an American corporation for infringement of an Israeli copyright, and where the development of the American corporation's product, which worked in tandem with the plaintiff's product, took place overseas and was sold to a Turkish corporation for use in trading on a U.S. exchange, the court held that it had no subject matter jurisdiction over plaintiff's claim. See Quantitative Fin. Software, 41 U.S.P.Q. 2d at 1766. The court explained that:

[T]he fact that a trade [accomplished with the aid of defendant's and plaintiff's product] takes place in the United States does not mean that infringement, i.e., a violation of one of the exclusive rights of the owner of copyright, 17 U.S.C. § 106, occurred in the United States, just because the foreign party to the trade may be using, in its computer program, information in which plaintiff has a copyright.

Id. This "Lex Protectionis" rule is in contrast to the recent recommendations of the European Commission, which advances the "country of origin" theory in its Green Paper on Copyright and Related Rights in the Information Society. See Copyright and Related Rights in the Information Society: Green Paper from the Commission to the European Council, COM(95)382 final; Don Beiderman, Copyright Trends: With Friends Like These..., 17 ENT. & SPORTS LAW 3, 7 (1999). For a further discussion of choice of law issues in the context of international copyright disputes, see Graeme W. Austin, Domestic Laws and Foreign Rights: Choice of Law in Transnational Copyright Infringement Litigation, 23 COLUM.-VLA J.L. & ARTS 1 (1999).

67. The Restatement discusses the limits of a country's authority to exercise jurisdiction over activities of non-residents. Restatement (Third) of the Foreign Relations Law of the United States § 401 (1986). There must first be: (1) jurisdiction to prescribe; (2) jurisdiction to adjudicate; and (3) jurisdiction to enforce. See id.; see also Rice, supra note 63, at 431.

of contributory and vicarious infringement where those acts provided the means by which direct infringement occurred in the United States. ⁶⁸

In GB Marketing USA, Inc. v. Gerolsteiner Brunnen GmbH & Co., 69 the District Court for the Western District of New York addressed the extraterritorial reach of the Copyright Act through its analysis of subject matter jurisdiction.⁷⁰ Plaintiff claimed that a German company had contributed to the infringement of its copyrights by affixing, abroad, copyrighted labels that it had no authority to use, on water bottles that were marketed and sold in America.⁷¹ Defendant moved to dismiss for lack of subject matter jurisdiction, claiming that the Copyright Act did not reach its activities abroad.⁷² The district court, noting that defendant was alleged to have sold the infringing bottles to a third party with the "knowledge and intent that the water would then be exported to the United States and sold here," went on to find that it had subject matter jurisdiction over the claim.⁷³ The court further found, using reasoning reminiscent of the "effects test" used to determine personal jurisdiction over foreign defendants,74 that it would be fair to adjudicate the claim against it because its acts, done abroad, "are intended to, and do, have an effect within the United States."⁷⁵ Indeed, the court went on, "it is precisely because the copyright statues are aimed at infringement in the United

68. See, e.g., Armstrong v. Virgin Records, Ltd., 91 F. Supp. 2d 628, 635-36 (S.D.N.Y. 2000) (finding that jurisdiction may exist over act of contributory or vicarious infringement where subsequent act of infringement took place in the United States); Blue Ribbon Pet Prods., Inc. v. Rolf C. Hagen (USA) Corp., 66 F. Supp. 2d 454, 462 (E.D.N.Y. 1999) (finding that acts of contributory or vicarious infringement in Canada may provide basis for liability in the U.S. where defendant knew or should have known that the other could be expected to infringe); ITSI T.V. Prods., Inc. v. California Auth. of Racing Fairs, 785 F. Supp. 854, 864 (E.D. Cal. 1992) (noting possibility that a defendant acting outside the U.S. may be held liable for contributory or vicarious infringement). For a fuller collection of cases, see also Dinwoodie, *supra* note 13, at 529.

- 69. GB Marketing USA, Inc. v. Gerolsteiner Brunnen GmbH & Co., 782 F. Supp. 763 (W.D.N.Y. 1991).
 - 70. Id. at 772.
 - 71. Id.
 - 72. Id.
 - 73. Id. at 773.
- 74. See Restatement (Second) of Conflict of Laws § 37 (1965) [hereinafter Restatement (Second)].
 - 75. *GB Marketing*, 782 F. Supp. at 773.

statues are aimed at infringement in the United States that the court must also consider the location of the *effect* of [defendant's] alleged action, i.e., the location of the ultimate direct infringement."⁷⁶

Similarly, in Metzke v. May Department Stores Co.,77 an American plaintiff, Ms. Metzke, sued her distributor for vicarious and contributory infringement of her copyrighted pewter potpourri jars.⁷⁸ The distributor, May Department Stores Co. ("May"), had offices in Taiwan which coordinated May's Taiwanese vendors and negotiated contracts between the corporate division of May ("MMC") and those vendors.⁷⁹ MMC, in turn, served as a "conduit" for May's retail division for products manufactured outside of the United States, and all imported goods for May's retail division were purchased through MMC.80 MMC had arranged for a Taiwanese company to copy Ms. Metzke's original copyrighted works for May stores, but the "knock-offs" found their way to non-May distributors in the U.S. and were sold here.81 On the defendant's motion for summary judgement, the district court found that no claim for vicarious infringement may lie because plaintiff could not prove the first element of the claim, namely that the defendant had the right and ability to supervise the infringing activity of another.82

As to contributory infringement, however, the court denied defendant's motion. In so doing, the court addressed defendant's argument that, because the direct infringement of the jars occurred in Taiwan, and is thus not actionable under the Copyright Act, there can be no contributory infringement.⁸³ The court agreed that since U.S. copyright law generally does not have extraterritorial effect, May could not be held liable for the direct infringement of the jars.⁸⁴ However, the court held that May could be liable, "if it knew or should have known that

^{76.} *Id*

^{77.} Metzke v. May Dep't Stores Co., 878 F. Supp. 756 (W.D. Pa. 1995).

^{78.} Id. at 758.

^{79.} Id.

^{80.} Id.

^{81.} Id. at 760.

^{82.} *Id.* For similar reasons, Robin des Bois would likely escape liability for vicarious infringement.

^{83.} Metzke, 878 F. Supp. at 760.

^{84.} *Id*.

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[the direct infringer's] copies of Ms. Metzke's designs would be distributed by non-May retailers in the United States."85 The court disposed of May's argument that it could not have known that non-May stores would sell the products because it did not so intend by calling the reasoning a "non sequitur."86 Having found that its part in plaintiff's injury was actionable under the Copyright Act, the defendant was obliged to face adjudication in the United States.87

In much the same way, our federal court in California would likely reach the same conclusion against Robin des Bois, at least as to its contribution to infringing activity within the U.S.⁸⁸ With the aid of precedent set by *Napster*, the court would reason that the very nature of Robin des Bois' business implies that it "knew or should have known" that its activities would lead to direct infringement of plaintiff's copyrights in the United States. The success of its business, much like Napster's, will have depended on its widespread popularity.89 Moreover, the case would be an easier one than *Metzke*, because the infringing activity would come subsequent to its facilitation, not before, and would indeed be encouraged by the file-sharing service. Robin des Bois could not claim it was surprised that its service ended up in the hands of unintended consumers, as by design, its populist service has no unintended consumers. Indeed, as the GB Marketing court observed, Robin des Bois' purposeful injection of its service into the American

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^{85.} *Id.* at 761 (citing 3 DAVID NIMMER & MELVILLE B. NIMMER, NIMMER ON COPYRIGHTS § 12.04[A][2][b] (1994)).

^{86.} Id.

^{87.} Id. at 762.

^{88.} As noted above, the district court would likely dismiss the claims of contributory infringement, where the predicate act of direct infringement takes place abroad, for lack of subject matter jurisdiction or for failure to state a claim under the Copyright Act. *See* Armstrong v. Virgin Records, Ltd., 91 F. Supp. 2d 628, 635 (S.D.N.Y. 2000).

^{89.} The district court would certainly engage in fact finding regarding Robin des Bois' intention to market to an American consumer base. Where jurisdictional and substantive issues intertwine, "the question of jurisdiction is dependent on the resolution of factual issues going to the merits." ITSI T.V. Prod., Inc. v. California Auth. of Racing Fairs, 785 F. Supp. 854, 858 (E.D. Cal. 1992). That analysis, though equally pertinent to the discussion of subject matter jurisdiction, overlaps with the inquiry into the court's personal jurisdiction and is discussed below in that context.

market would make its argument that the Copyright Act does not extend to its facilitating activities unavailing.⁹⁰

B. Personal Jurisdiction

The defendant in *Metzke* was based in the U.S., and did not raise the defense of lack of personal jurisdiction.⁹¹ Therefore, the issue of the court's subject matter jurisdiction having been decided, no defense of lack of personal jurisdiction was raised. Robin des Bois, however, is a French company, and it will surely assert that, even if its activities are actionable under the Copyright Act, the District Court for the Northern District of California cannot exercise personal jurisdiction over it.

As no specific federal statute governs personal jurisdiction under the Copyright Act, courts look to the long-arm statute of the state in which they sit. ⁹² The California long-arm statute is typical of long-arm statutes in other states that render jurisdiction coextensive with the outer limits of due process. ⁹³ Therefore, to survive due process scrutiny, the exercise of jurisdiction must "not offend 'traditional notions of fair play and substantial justice." ⁹⁴ Put another way, the defendant's activities must be such that he "should reasonably anticipate being hauled into court in the United States."

There are two types of personal jurisdiction over a defendant: general and specific.⁹⁶ General jurisdiction exists where a defendant's activities in the state, regardless of whether they are related to the cause of action, are "substantial" or "continuous and systematic." In all likelihood, foreign companies implicated in our hypothetical would not be subject to general juris-

^{90.} See GB Marketing USA, Inc. v. Gerolsteiner Brunnen GmbH & Co., 782 F. Supp. 763, 773 (W.D.N.Y. 1991).

^{91.} Metzke, 878 F. Supp. at 758.

^{92.} See Blue Ribbon Pet Prods., Inc. v. Rolf C. Hagen (USA) Corp., 66 F. Supp. 2d 454, 459 (E.D.N.Y. 1999).

^{93.} See Cal. Code Civ. P. § 410.10 ("A court of this state may exercise jurisdiction on any basis not inconsistent with the Constitution of this state or of the United States."). See also Rano v. Sipa Press, Inc., 987 F.2d 580, 587 (9th Cir. 1993).

^{94.} International Shoe Co. v. Washington, 326 U.S. 310, 316 (1945) (quoting Milliken v. Meyer, 311 U.S. 457, 463 (1940)).

^{95.} World-Wide Volkswagen Corp. v. Woodson, 444 U.S. 286, 297 (1980).

^{96.} See Rano, 987 F.2d at 587.

^{97.} See id.

diction here.⁹⁸ Therefore, this analysis focuses on specific jurisdiction. Specific jurisdiction lies when: (1) the foreign defendant performs an act by which he purposefully avails himself of the privilege of conducting activities in the forum; (2) the claim arises out of or results from the defendant's forum related xtivities; and (3) the exercise of jurisdiction is reasonable.⁹⁹ Another way to frame the first inquiry is to ask whether the defendant purposefully directs his activity into the forum.¹⁰⁰ If he has, he has invoked that forum's protection and should reasonably expect to defend himself there.¹⁰¹ In the context of torts, the effects test, though less often applied to intellectual property disputes, is perfectly appropriate to utilize as well.¹⁰² Under the effects test, the due process clause will not be offended and a court may exercise jurisdiction over the defendant if he caused an effect in the forum by an act done elsewhere that is related to the plaintiff's cause of action.¹⁰³

For the most part, cases adjudicating whether jurisdiction can lie over a defendant residing outside the forum state who utilizes the Internet to conduct its business have been brought pursuant to the Lanham Act¹⁰⁴ in the context of domain name trademarks disputes.¹⁰⁵ Because of the unique nature of the tort of contributory infringement, these cases are therefore of

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^{98.} See Helicopteros Nacionales de Colom., S.A. v. Hall, 466 U.S. 408, 414 (1984) (finding that personal jurisdiction exists when there are sufficient contacts between the foreign corporation and the forum state or where the cause of action arises out of that corporation's activities). See also Rice, supra note 63, at 436 (general jurisdiction has been accorded less attention in Internet related cases).

^{99.} See Cybersell, Inc. v. Cybersell, Inc., 130 F.3d 414, 416 (9th Cir. 1997); Rano, 987 F.2d at 588; Zippo Mfr. Co. v. Zippo Dot Com, Inc., 952 F. Supp. 1119, 1122-23 (W.D. Pa. 1997).

^{100.} See Cybersell, 130 F.3d at 417.

^{101.} See id. at 416-17.

^{102.} See Cybersell, 130 F.3d at 420 (rejecting defendants arguments on the facts); World-Wide Volkswagen Corp. v. Woodson, 444 U.S. 286, 297-98 (1980); Core-Vent Corp. v. Nobel Indus., AB, 11 F.3d 1482, 1486 (9th Cir. 1993); Panavision Int'l, L.P. v. Toeppen, 938 F. Supp. 616, 621 (C.D. Cal. 1996); RESTATEMENT (SECOND), supra note 74, § 37 (jurisdiction over a foreign defendant does not offend due process if he caused an effect in the forum by an act done elsewhere that is related to the plaintiff's cause of action).

^{103.} Restatement (Second), supra note 74, § 37.

^{104.} Trademark Act of 1946, 15 U.S.C. §§ 1051-1129 (2000) (popularly known as the Latham Act).

^{105.} See infra note 114.

limited utility to this analysis. Nonetheless, they are instructive because our court will take guidance from them, thus, several cases are discussed below.

Zippo Manufacturing Co. v. Zippo Dot Com, Inc.¹¹¹¹ is considered by courts and commentators alike to be the first to lay out a comprehensive analytical framework to test personal jurisdiction based on Internet activity.¹¹¹ In Zippo, Judge McLaughlin analyzed a California corporation's contacts with the Commonwealth of Pennsylvania in order to determine whether specific personal jurisdiction existed over the defendant.¹¹¹³ After setting out the traditional rules for determining jurisdiction, established by International Shoe Co. v. Washington,¹¹¹³ Hanson v. Denckla,¹¹¹³ World-Wide Volkswagen v. Woodson,¹¹¹ Helicopteros Nacionales de Colombia, S.A. v. Hall¹¹² and Burger King Corp. v. Rudzewicz,¹¹¹³ the court took guidance from several cases dealing with jurisdiction over Internet-based companies.¹¹¹⁴ The court noted that, while "the

^{106.} Zippo Mfr. Co. v. Zippo Dot Com, Inc., 952 F. Supp. 1119 (W.D. Pa. 1997).

^{107.} See Cybersell, 130 F.3d at 419; Rice, supra note 63, at 464.

^{108.} Plaintiffs in *Zippo* conceded that the court did not have general jurisdiction over the defendant. *Zippo*, 952 F. Supp. at 1125-26.

^{109.} International Shoe Co. v. Washington, 326 U.S. 310, 316 (1945).

^{110.} Hanson v. Denckla, 357 U.S. 235 (1958).

^{111.} World-Wide Volkswagen v. Woodson, 444 U.S. 286, 294 (1980).

^{112.} Helicopteros Nacionales de Colom., S.A. v. Hall, 466 U.S. 408, 414 (1984).

^{113.} Burger King Corp. v. Rudezewicz, 471 U.S. 462 (1985).

^{114.} See Zippo Mfg. Co. v. Zippo Dot Com, Inc., 952 F. Supp. 1119, 1124-25 (W.D. Pa. 1997) (discussing CompuServe, Inc. v. Patterson, 89 F.3d 1257, 1266-67 (6th Cir. 1996) (plaintiff purposefully directed business activities to forum state by knowingly entering into contract there and deliberately and repeatedly transmitting files into forum state)); Maritz, Inc. v. Cybergold, Inc., 947 F. Supp. 1328, 1333 (E.D. Mo. 1996) (jurisdiction found where there was active solicitation and promotional activity to develop mailing list for upcoming Internet service); Inset Sys., Inc. v. Instruction Set, 937 F. Supp. 161, 165 (D. Conn. 1996) (advertising on website accessible in plaintiff's forum was sufficient to confer jurisdiction in part because continuous nature of Internet advertising may be characterized as "repetitive" for purposes of satisfying Connecticut long arm statute): Bensusan Restaurant Corp. v. King. 937 F. Supp. 295, 301 (S.D.N.Y. 1996) (no jurisdiction where non-interactive website merely available outside defendant's jurisdiction); Pre-Kap, Inc. v. System One, Direct Access, Inc., 636 So. 2d 1351, 1353 (Fla. Dist. Ct. App. 1994) (no jurisdiction over consumer of services on the Internet where the consumer is not soliciting or marketing products). Among these cases, Inset

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cases are scant," their review warranted the conclusion that "the likelihood that personal jurisdiction can be constitutionally exercised is directly proportionate to the nature and quality of commercial activity that an entity conducts over the Internet."¹¹⁵ The court went on to determine, based on this

has been most thoroughly criticized as an example of the outer limit of jurisdictional analysis. *See*, *e.g.*, Rice, *supra* note 63, at 462-63 (providing a comprehensive survey of cases dealing with personal jurisdiction over companies utilizing the Internet).

115. Zippo, 952 F. Supp. at 1124. Perhaps the most interesting aspect of the Zippo opinion, albeit one that is beyond the focus of this Article, is the court's response to the defendant's contention that its contacts with Pennsylvania were not unlike the defendant's in World-Wide Volkswagen. Id. at 1126-27. In the seminal case of World-Wide Volkswagen, the Supreme Court determined that the defendant's contacts with the forum state were "fortuitous." World-Wide Volkswagen, 444 U.S. at 295. In that case, a couple who purchased a car in New York were injured while driving through the State of Oklahoma and brought suit there. Id. at 288. The manufacturer of the vehicle did not sell its vehicles in Oklahoma and had not attempted to establish its business there. Id. at 295.

Defendant in *Zippo* argued that its contacts with Pennsylvania were similarly "fortuitous" because a Pennsylvania resident happened upon its website. *Zippo*, 952 F. Supp. at 1126. In rejecting defendant's argument, the court, in dicta, posited that:

Dot Com's [defendant's] contacts with Pennsylvania would be fortuitous within the meaning of *World-Wide Volkswagen* if it had no Pennsylvania subscribers and an Ohio subscriber forwarded a copy of a file he obtained from Dot Com to a friend in Pennsylvania or an Ohio subscriber brought his computer along on a trip to Pennsylvania and used it to access Dot Com's service.

Id. It is not unlikely that this is precisely the type of argument that would be made by a true peer-to-peer Internet music service. Unlike Napster, true peer-to-peer applications do not need the aid of a central server to enable personal computers ("PCs") to link together. See, e.g., Rocky Road, supra note 7 (For MusicCity, Kazaa and all the Gnutella-based companies such as LimeWire LLC, and BearShare, central servers do not make connections between PCs on the network – rather, PCs are themselves "deputized on the fly to play temporary roles as network traffic cops. . . .").

Commentators have observed that the removal of the central server from the peer-to-peer infrastructure may insulate developers of such applications from litigation because, unlike Napster, no centralized list of copyrighted files is maintained by the developer, and no direct assistance is provided to the unauthorized trading of copyrighted works. *See* Bailey, *supra* note 4, at 473, 476, 481 & 516 (pure peer-to-peer services leave only individuals as defendants – there is no "Gnutella, Inc.," just hackers who derive no financial gains from putting the Gnutella program on the Internet). Bailey's

guiding principle, that personal jurisdiction is proper over a defendant entering into contracts with residents of the forum jurisdiction "that involve the knowing and repeated transmission of computer files over the Internet." Conversely, "a passive website that does little more than make information available to those who are interested in it" is not amenable to jurisdiction. Somewhere in between the two ends of the spectrum are "interactive Web sites where a user can exchange information with the host computer. In these cases, the exercise of jurisdiction is determined by examining the level of interactivity and commercial nature of the exchange of information [occurring on the site]." Ultimately, the *Zippo* court determined that the defendant was conducting business over the Internet with Pennsylvania residents by contracting with over 3,000 consumers and seven Internet access providers to deliver news,

suggestion that only criminal sanctions will be effective against peer-to-peer originators may shortly be tested in the international arena. See id.

The Council of Europe Ministers' Deputies have recently announced their approval of the Convention on Cybercrime. See Press Release, Council of Europe, First International Treaty to Combat Crime in Cyberspace Approved by Ministers' Deputies (Sept. 19, 2001), available at http://press.coe.int/cp/2001/646a(2001).htm [hereinafter Press Release]. The Convention, scheduled to be open for signature in late November 2001, will go into force when five states, at least three of which are members of the Council of Europe, have ratified it. See Convention on Cybercrime, Nov. 23, 2001, Europ. T.S. No. 185. According to the Council of Europe, the Convention will be the first international treaty on crimes committed in cyberspace, dealing particularly with copyright infringement, among other pressing legal issues created by the proliferation of the Internet. See Press Release, supra note 115. On the other hand, however, these companies must still have some hardware and Internet connections in order to maintain their relationships with advertisers and distribution sources such as CNET Download.com. See Rocky Road, supra note 7. The real question may be not whether one can find the facilitator of the peer-to-peer infringement, but whether the facilitator's activities rise to the level of actionable contribution under the Napster formulation.

116. Zippo, 952 F. Supp. at 1124 (this category is understood as representing "active" websites).

117. *Id.* A passive website would not ordinarily provide a means by which the accessor of the site might interact with the site. *See* Rice, *supra* note 63, at 464. There are a collection of cases where courts refused to find jurisdiction over "purely passive" websites. *See* Jeffrey P. Cunard & Jennifer B. Coplan, *Selected Topics in eCommerce Law, in* MCLE Marathon 2000, at 445-46 (PLI N.Y. Practice Skills Course, Handbook Series No. F0-007N, 2000).

118. Zippo, 952 F. Supp. at 1124.

and that the court had personal jurisdiction over it.¹¹⁹ This active/passive/interactive analysis employed by the court has been used as an aid by subsequent courts in determining jurisdiction.¹²⁰

Taking guidance from the Zippo court, as well as decisions by the Court of Appeals for the Second Circuit and Court of Appeals for the Sixth Circuit, 121 the Ninth Circuit in Cybersell, Inc. v. Cybersell, Inc., 122 found that a website in Florida, which did nothing to encourage people in Arizona (plaintiff's domicile) to access its site, was not amenable to personal jurisdiction in a trademark infringement case. 123 No "hits" were made to the website in Arizona, save the plaintiff's own, no "800" number was available for people from Arizona to call, and the Florida business was mainly generated from personal contacts rather than the Internet. 124 The Cybersell court also rejected plaintiff's "effects" test argument, distinguishing cases in which jurisdiction was found on the facts of the case. 125

However, on the facts of our hypothetical, the effects test would serve to keep Robin des Bois in California federal court. Indeed, the facts for finding jurisdiction over Robin des Bois are stronger than those of *Panavision International*, *L.P. v. Toeppen*, where the District Court for the Central District of California, employing the effects test, found it proper to exer-

^{119.} *Id.* at 1126-27 (defendant had sold passwords to its 3,000 Pennsylvania subscribers and contracted with providers to furnish its services in Pennsylvania). The *Zippo* court found that it could exercise jurisdiction over defendants under a specific provision of the Pennsylvania long arm statute allowing for jurisdiction over non-residents who contract "to supply services or things in this Commonwealth." *Id.* at 1122 (citing 42 PA. CONS. STAT. ANN. § 5322(a)(2) (1992)). However, the court emphasized that "even if Dot Com's [defendant's] conduct did not satisfy a specific provision of the statue, we would nevertheless be authorized to exercise jurisdiction to the 'fullest extent allowed under the Constitution of the United States." *Id.* (quoting 42 PA. CONS. STAT. ANN. § 5322(B) (1992)).

 $^{120.\} See$ Cybersell, Inc. v. Cybersell, Inc., 130 F.3d 414 (9th Cir. 1997); iAccess, Inc. v. Webcard Tech., 2002 WL 99651 (D. Utah Jan. 24, 2002).

^{121.} The Ninth Circuit examined *Bensusan Restaurant Corp. v. King*, 937 F. Supp. 295 (S.D.N.Y. 1996), *aff'd*, 126 F.3d 25 (2d Cir. 1997) and *Compu-Serve, Inc. v. Patterson*, 89 F.3d 1257 (6th Cir. 1996).

^{122.} Cybersell, 130 F.3d at 420.

^{123.} Id. at 419.

^{124.} Id.

^{125.} *Id.* at 420.

^{126.} Panavision Int'l, L.P. v. Toeppen, 938 F. Supp. 616 (C.D. Cal. 1996).

cise personal jurisdiction over a defendant who merely registered a website in the name of plaintiff's business, hoping to extort a fee from plaintiff, when and if plaintiff should decide to take its business on-line. ¹²⁷ In *Panavision*, the defendant did no business through the Internet, and the court made plain that its decision did not hinge on the analysis of Bensusan Restaurant Corp. v. King and CompuServe, Inc. v. Patterson, 128 the cases examined in Cybersell. 129 Instead, the court found that the defendant's registration of the domain name at issue was done "with the knowledge that the names belonged to [plaintiff] and with the intent to interfere with [plaintiff's] business."130 All that the court seemed to find pertinent was the defendant's knowledge that his actions would cause an effect on plaintiff's business. Robin des Bois, on the other hand, under our Napster-like facts, not only runs a business which derives a profit from the exploitation of A&M's music, but also knows that it is interfering with A&M's existing business.¹³¹

Similarly, the defendant's knowledge of the harm he was causing provided the impetus in the most recent case in California which used the effects test to find personal jurisdiction over a defendant using the Internet.¹³² In *Pavlovich v. Superior Court*, the defendant was the president of a start-up technology company that posted decryption computer programs by misappropriating the trade secrets of a company specializing in

^{127.} Id. at 621.

^{128.} *Id.* at 622. *See also* Compuserve, Inc. v. Patterson, 89 F.3d 1257 (6th Cir. 1996); Bensusan Restaurant Corp. v. King, 937 F. Supp. 295 (S.D.N.Y. 1996).

^{129.} Cybersell, 130 F.3d at 417.

^{130.} *Panavision*, 938 F. Supp. at 621.

^{131.} See supra note 6 (discussing new Internet music distribution ventures by major labels).

^{132.} See Pavlovich v. Superior Court, 109 Cal. Rptr. 2d 909 (Cal. Ct. App. 2001). While Pavlovich was decided on August 31, 2001, the procedural history of this case indicates that its ruling on personal jurisdiction is far from final. Indeed, Pavlovich has been successful in convincing the Supreme Court of California to review the ruling of the Court of Appeals on December 12, 2001. See Paylovich v. Santa Clara County Superior Court, 114 Cal. Rptr. 2d 611 (Cal. 2001). See also David McGuire, DVD Crypto Defendant Appeals to Court.Supreme Newsbytes (Jan. 16. 2002). California http://www.newsbytes.com. Arguments are expected to be heard sometime later this year. The case has come to be called by some a "bellwether on the issue of cyberjurisdiction." *Id*.

digital versatile disk ("DVD") encryption technology. 133 Defendant also aimed to create an unlicensed DVD player that would use the technology developed by his company to decrypt proprietary DVD data in order to allow the unauthorized copying and transmission of movies in the DVD format.¹³⁴ Deposition testimony revealed that defendant knew that licenses were required to use DVD technology, 135 he knew that the computer technology industry is centered in California, 136 and he knew that California is the center of the motion picture industry. 137 The court dispensed with the defendant's argument that because he did not specifically know the identity and location of the plaintiff when he undertook his acts, he was not subject to personal jurisdiction by holding that such specific knowledge is not a requirement.¹³⁸ Citing *Panavision*, the appellate court noted that the "purposeful availment' requirement is satisfied where a defendant's intentional conduct causes harmful effect within the state."139 The court went on to hold that it had personal jurisdiction over the defendant because "he knew, or should have known, that the DVD republishing and distribution activities he was illegally doing and allowing to be done through the use of his Web site, while benefiting him, were injuriously affecting the motion picture and computer industries in California."140

From the cases examined above, it is easy to see how the inquiry into whether a court has personal jurisdiction over a defendant is quite similar to the analysis of subject matter jurisdiction. Indeed, both effects tests hinge on the defendant's knowledge that his actions will cause negative consequences to the plaintiff. In the context of our contributory infringement hypothetical, this means that A&M will have to demonstrate that Robin des Bois knew, or should have known, that its activities outside the United States would cause A&M harm. Here again, the fact that A&M, heeding *Napster*, has sent

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^{133.} Pavlovich, 109 Cal. Rptr. 2d, at 911.

^{134.} See id. at 911-12.

^{135.} See id. at 912.

^{136.} See id.

^{137.} See id. at 915.

^{138.} See id. at 918.

^{139.} See Pavlovich, 109 Cal. Rptr. 2d at 915.

^{140.} *Id*.

Robin des Bois mtice that plaintiff's copyrighted material can be found on Robin des Bois' website and has demanded that it be removed, coupled with the fact that the peer-to-peer file sharing technology was structured to allow the exchange of copyrighted material, will lead the court to the inescapable conclusion that it will not offend due process to exercise personal jurisdiction over Robin des Bois. 142

In addition, although, as stated earlier, no court has as yet applied the *Zippo* continuum to copyright infringement cases, the court would likely find that the Robin des Bois website was active in the sense that, by virtue of its set-up, it materially contributes to the direct infringing activity of its users. Indeed, it would be odd at best for a court to conclude that a website was passive, yet that it materially contributed to infringing activity.

C. Liability

Finally, having found subject matter and personal jurisdiction, with the aid of the *Napster* precedent, our district court in California will have no trouble issuing a preliminary injunction against Robin des Bois.¹⁴³ Determining whether one causes an effect in the plaintiff's chosen forum, for purposes of subject matter and personal jurisdiction, is conceptually similar to determining whether he "knows of and contributes to" a direct violator's infringement.¹⁴⁴ Thus, personal jurisdiction analysis,

^{141.} See Napster II, 239 F.3d 1004, 1020-21 (9th Cir. 2001).

^{142.} Once a plaintiff has demonstrated that the defendant intended to cause an effect in his chosen forum, he must go on to show that jurisdiction would be reasonable (the third prong of the specific jurisdiction inquiry). Practically speaking, many courts collapse the analysis of the two prongs into one. If they go on to analyze the reasonableness prong, it is almost a foregone conclusion that they will find the exercise of jurisdiction reasonable. For this reason, we do not take up this analysis here.

^{143.} The preliminary injunction would not, however, be applicable outside of the United States. For a judgment to be enforceable extraterritorially, it must be executory and final. FED. R. CIV. P. 65.

^{144.} At least one court has distinguished the cases finding jurisdiction on the basis that the connection between the jurisdictional inquiry and the cause of action present in those cases was absent. In *Digital Control Inc. v. Boretronics Inc.*, No. C01-0074L, 2001 U.S. Dist. LEXIS 14600, at *1 (W.D. Wash. Sept. 7, 2001), the court refused to exercise personal jurisdiction over a Minnesota defendant who allegedly infringed plaintiff's patent in transmitters designed for use in remote drilling. The defendant's contacts with the

like the analysis of subject matter jurisdiction, will converge with the court's ultimate analysis of whether plaintiff has shown that it is entitled to a preliminary injunction. As a practical matter, when our California district court finds that it can take subject matter jurisdiction over the claim, and that it can also exercise personal jurisdiction over Robin des Bois, the finding that plaintiffs will likely succeed in proving that Robin des Bois knows that infringing material is beated on its system will be a foregone conclusion.

And because Robin des Bois functions much like Napster, in following the *Napster* decision, the court will conclude that it "materially contributed" to the infringing activity by providing "the site and facilities' for direct infringement." After all, as in *Napster*, without Robin des Bois' provision of the software (which makes file-swapping possible) and without its search engine, servers and means of establishing a connection between users' computers, Robin des Bois' users could not find and download the music they want with the ease the company hopes to provide. 146

Having found that plaintiff will likely succeed on the merits, the court will issue a preliminary injunction structured much like the one used in *Napster*. Of course, because the Copyright Act does not have extraterritorial effect, the court will not compel Robin des Bois to take down its service outside of the

State of Washington amounted to activities that had a national scope – the defendant advertised in two industry journals and established a website on which it offered the product for sale. *Id.* at *3. It also maintained a toll free number that could be accessed by Washington residents. *Id.* The court, noting that no cases on point were to be found in the federal circuit, distinguished *Inset Sys., Inc. v. Instruction Set*, 937 F. Supp. 161 (D. Conn. 1996) and *Zippo Mfg. Co. v. Zippo Dot Com, Inc.*, 952 F. Supp. 1119 (W.D. Pa. 1997), on the ground that "those cases . . . generally involve claims that the Internet advertisement itself infringed on a patent or trademark." *Id.* at *4. The court went on to apply the "web site plus" rule where:

Until the advertiser is actually faced with and makes the choice to dive into a particular forum, the mere existence of a worldwide web site, regardless of whether the site is active or passive, is an insufficient basis on which to find that the advertiser has purposely drected its activities at residents of the forum state.

Id. at *7.

^{145.} Napster II, 239 F.3d at 1022.

^{146.} Napster I, 114 F. Supp. 2d 896, 920 (N.D. Cal. 2000).

United States. Nonetheless, the French company will have been deprived of a customer base that cannot seem to get enough free music and ultimately, of a great source of revenue. Without the impressive American user-base, Robin des Bois will eventually be forced to leave the forest.

IV. CONCLUSION

To date, the issues posited by our fictitious lawsuit against Robin des Bois remain unexamined outside of the hypothetical analyzed in the Article. It would not be surprising, however, if real defendants based outside the United States, such as Grokster, Ltd. Empowerment BV, or future defendants as yet unknown, raised the defense of lack of subject matter and personal jurisdiction in copyright infringement lawsuits filed against them. It will be interesting to observe whether, on a motion to dismiss for lack of jurisdiction, the theories asserted by the litigants will be similar to the effects test discussed previously. Equally interesting will be whether, having taken jurisdiction over the claim, the court will extend the effects analysis to the substantive matter of granting an injunction against the would-be contributory infringer.

Regardless of how current litigation develops, however, it appears clear that sooner rather than later, a Robin des Bois type service will spring up outside U.S. borders. The issues we raise concerning contributory copyright infringement litigation initiated in the U.S. against such a service will have far reaching implications that will reverberate, much like the Internet itself, on an international level. One way or the other, it seems inevitable that they will be addressed.

^{147.} A file-swapping service that is available free of charge will primarily survive on advertising dollars. *See* UMG Recordings, Inc. v. MP3.com, Inc., 92 F. Supp. 2d 349, 351 (S.D.N.Y. 2000).

^{148.} Grokster's principal place of business is Nevis, West Indies. See Metro-Goldwyn-Mayer, Inc. v. Grokster, Ltd., No. 01-8541 (C.D. Cal. filed Oct. 2, 2001); Steven Bonisteel, If Morpheus Is Illegal, So is the Rest of the Net-EEF, Newsbytes (Feb. 26, 2002), at http://www.newsbytes.com/news/02/174778.html; supra note 8.

^{149.} Empowerment's principal place of business is Amsterdam, The Netherlands. See Grokster. No. 01-8541.

^{150.} As of this writing, it appears that the defendants in *Grokster* have chosen to attack the allegation against them on a substantive level by asserting the Betamax defense. *See supra* note 36; Bonisteel, *supra* note 148.

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IT BEGAN AT BROOKLYN: EXPANDING BOUNDARIES FOR FIRST-YEAR LAW STUDENTS BY INTERNATIONALIZING THE LEGAL WRITING CURRICULUM

Diane Penneys Edelman*

"[L]aw must be viewed today through a global lens, and . . the way we think about and teach the law must embrace that perspective." 1

I. INTRODUCTION

Teach international law to first-year law students? Why? There are several answers to this question. Perhaps the most practical reason is that international law is becoming so important to our lives as lawyers and educators (and, in fact, to our lives in general) that we can no longer dismiss this idea as one that is controversial or impractical. By introducing stu-

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^{1.} Norman Dorsen, Thinking and Teaching About Law in a Global Context as an Exercise in Common Enterprise, Remarks at the Association of American Law Schools Annual Meeting (Jan. 8, 1998).

dents early on to concepts of international law, we teach them that law extends beyond the boundaries of traditional practice, and show them that the law is as diverse as the peoples who create it. The subject matter of such a course can be as farreaching as the professor's imagination: international human rights, transboundary pollution, recognition of new states and outer space law are but examples of topics that can be covered.

Teachers of doctrinal first-year courses should be encouraged to incorporate international law into their curricula, and a first-year legal writing program provides an excellent and easily adaptable venue for doing so. An introductory level international law legal writing program should strengthen the school's international law moot court teams² and increase student interest in the school's international and comparative law curriculum. Most importantly, this alternative offers variety to the first-year law student who is, usually, relegated to the traditional first-year substantive offerings and a traditional legal writing program. First-year law students relish taking control of their academic program, and the availability of an innovative or alternative course that incorporates international law gives students what may be their only chance to elect a course in an otherwise prescribed curriculum.

Although a number of law schools offer three or foursemester legal writing programs, the majority of law schools

^{2.} Many law schools, both in the United States and abroad, participate in the Philip C. Jessup International Law Moot Court Competition, which was established in 1959 in honor of the scholar and former judge of the International Court of Justice. See International Law Students Association, About the Philip C. Jessup International Law Moot Court Competition, at http://www.ilsa.org (last visited Feb. 18, 2002). In recent years, additional international law moot court competitions, such as the Inter-American Human Rights Moot Court Competition (sponsored by Washington College of Law, American University), at http://www.wcl.american.edu/humright/ mcourt/; Niagara International Law Moot Court Tournament (sponsored by Canada/United States Law Institute and Case Western University School of Law), at http://lawwww.cwru.edu/academic/moot_mock.htm; Manfred Lachs Space Law Moot Court Competition (sponsored by International Institute of Space Law of the International Astronautical Federation), http://www.iafastro.com/iisl/MootCourt2001.htm: International mental Moot Court Competition (sponsored by Stetson University College of Law), at http://www.law.stetson.edu/excellence/mootct/moot.htm: Willem C. Vis International Commercial Arbitration Moot (sponsored by Pace University School of Law), at http://www.cisg.law.pace.edu/vis.html, have become popular at American law schools as well.

only offer two-semester legal writing or legal research and writing programs.³ During the first semester of these programs, professors typically require students to prepare a variety of objective legal office memoranda, which students research and prepare for the purpose of advising a senior attorney regarding what decision to make or advice to provide in relation to a hypothetical legal problem.⁴ During the second semester, students move from objective to persuasive writing, and typically prepare one or more briefs to the court and present oral argument before a panel of moot court judges.⁵

Most commonly, and this is still by no means common, international law has been incorporated into the first-year curriculum by means of the typical first-year second semester moot court program.⁶ Brooklyn Law School has perhaps the first program of this kind, having introduced international law into the legal writing curriculum in the late 1970's.⁷ Several law schools, including Villanova University School of Law ("Villanova") and Syracuse University College of Law ("Syracuse"), have also pioneered first-year academic programs that include an international law moot court alternative to the traditional first-year legal writing curriculum.⁸

^{3.} See Ass'n of Legal Writing Dir. Legal Writing Inst., 2001 Survey Results, 4-5 (2001), available at http://www.alwd.org/resources/survey_results.htm#2001 (last visited Feb. 19, 2002).

^{4.} See American Bar Ass'n, Sourcebook on Legal Writing Programs 13 (1997) [hereinafter Sourcebook].

^{5.} See id. at 14, 28.

^{6.} See infra notes 7-8 and accompanying text.

^{7.} E-mail from Marilyn R. Walter, Professor of Law and Director, Legal Writing Program, Brooklyn Law School, to Diane Penneys Edelman, Assistant Dean for Legal Writing, Villanova University School of Law (Nov. 20, 2001, 15:20 EST) (on file with author).

^{8.} Syracuse offers an "International Law Firm" option for first-year legal writing students. Telephone Message from Richard S. Risman, Assistant Professor of Law and Director, Law Firm Program, Syracuse University College of Law, to Diane Penneys Edelman, Assistant Dean for Legal Writing, Villanova University School of Law (Nov. 5, 2001). Some law schools have added a substantive international law "perspectives" elective for first-year students, including Boston University School of Law, which offers a two-semester course in International Legal Process, The University of Michigan Law School, which offers Transnational Law as a first-year elective and New England School of Law, which has "internationalized" many of its traditional domestic law courses by offering grants to professors to do so. See Tom Stabile, The Innovators, NAT'L JURIST, Mar. 2000, at 25, 27-28; Linda Goodspeed,

Using the Villanova program as a model,⁹ this Article will focus on the fundamental concepts that must be taught in an international law moot court course, as well as the mechanics of offering and teaching international law moot court as an introductory level legal writing course. In addition, this Article will offer suggestions for integrating international law into the first semester legal writing program as well.

Specifically, Section II of this Article will introduce the sources of international law with which students in a first year "internationalized" legal writing program must become familiar. Section III describes how to select students, develop course materials and provide basic and supplemental instruction for the persuasive writing or moot court portion of the first-year legal writing program. Section IV addresses the relatively more simple task of introducing international law into a typical first semester, objective legal writing curriculum. Finally, Section V concludes that "internationalizing" the first-year legal writing curriculum is not only desirable, but is a necessary goal for preparing today's law students to be competent professionals in the new millennium.

II. THE SOURCES OF INTERNATIONAL LAW

Why is an international law moot court course so different from a traditional first-year moot court course? Simply put, it is primarily different because of the *type* of research involved; in other respects, students receive training in persuasive writing and oral advocacy similar to what they would receive in a

Stipend Boosts International Study at NE School of Law, Boston Bus. J., Nov. 12-18, 1999, at 38. Law book publishers are beginning to publish textbooks that can be used to teach international law to first-year students. See, e.g., Daniel G. Partan, The International Law Process: Cases and Materials (1992); Michael P. Scharf & John A. Barrett, Internationalizing the Domestic Curriculum (forthcoming 2002); Francisco Forrest Martin & Mark Tushnet, The Rights International Companion to Constitutional Law: An International Law Supplement (1999); Diane Penneys Edelman, The International Law Moot Court Handbook: A Guide to Persuasive Writing and Oral Advocacy for Students in International Law Moot Court Courses and Competitions (forthcoming) (on file with author).

^{9.} Of the programs referred to in this Article, the courses at Villanova and Syracuse are the only ones taught by full-time legal writing faculty.

traditional second or third-semester legal writing course.¹⁰ In addition, there are differences in the forum in which an international law moot court course is set. Rather than using a domestic appellate court, the international law moot court problem is set before a panel of the International Court of Justice ("ICJ"), which, in the real world, sits in The Hague, The Netherlands.¹¹

Consequently, the greatest challenge to a law student who elects to participate in an international law moot court program – whether by enrolling in a legal writing course or participating in the Philip C. Jessup International Law Moot Court Competition ("Jessup") as an upper class student – is mastery of the sources of international law that are applied by the ICJ. Unlike domestic law, where the student must grapple with the constitution-statute-case law hierarchy, the student of international law must become comfortable with treaties as well as the more amorphous concepts of "customary international law" and "general principles of law."12 These are the primary sources of international law, just as constitutions, statutes and cases are the primary sources of both federal and state domestic law. When it comes to secondary means for determining rules of domestic law, students in a traditional moot court class look to law reviews, treatises and digests. In contrast, the international law moot court student looks to both scholarly works and case law, both international and domestic,

^{10.} In fact, this course can be taught using a traditional legal writing textbook. See infra Part III.B. The only section of a traditional appellate brief that has no counterpart in an international law moot court brief is the standard of review, because the forum for this exercise is the International Court of Justice, which is a court of original jurisdiction that enters judgments from which there is no appeal. See Statute of the International Court of Justice, June 26, 1945, art. 60, 59 Stat. 1055, 1063, T.S. No. 993 [hereinafter ICJ Statute].

^{11.} See International Court of Justice, at http://www.icj-cij.org (last visited Feb. 18, 2002). See also Shabtai Rosenne, The World Court: What It Is and How It Works (5th ed. 1995). Other international tribunals, before which a hypothetical moot court exercise could be presented, include the International Criminal Tribunal for the Former Yugoslavia, the International Criminal Tribunal for Rwanda, the European Court of Human Rights, the Inter-American Court of Human Rights and a host of others. See The Project on International Courts and Tribunals, at http://www.pict-pcti.org/home.html (last visited Feb. 22, 2002).

^{12.} ICJ Statute, *supra* note 10, art. 38(1)(b)-(c).

as *secondary* means for determining rules of international law.¹³ Thus, it is crucial for the international law moot court professor to spend sufficient time at the beginning of the æmester making sure that students have a comfortable grasp of the following basic concepts before starting their research and writing project.

The sources of international law are defined in Article 38(1) of the Statute of the International Court of Justice ("ICJ Statute"), which lists the sources applied by the ICJ in deciding matters before the court. Although the ICJ Statute does not specifically address whether the sources have a hierarchic value as listed, scholars and the ICJ itself apply the sources in descending order. Students should be made aware that in international law there are both primary and secondary sources of law, just as there are in domestic law. The primary sources include international conventions, in international custom and the "general principles of law recognized by civilized"

- 13. See id. art. 38(1)(d); infra Part II.D.
- 14. Id. art. 38(1). Article 38 provides, in relevant part:
 - 1. The Court, whose function is to decide in accordance with international law such disputes as are submitted to it, shall apply:
 - (a) international conventions, whether general or particular, establishing rules expressly recognized by the contesting states;
 - (b) international custom, as evidence of a general practice accepted as law;
 - (c) the general principles of law recognized by civilized nations;
 - (d) subject to the provisions of Article 59, judicial decisions and the teachings of the most highly qualified publicists of the various nations, as subsidiary means for the determination of rules of law.
- *Id.* Article 59 states: "The decision of the Court has no binding force except between the parties and in respect of that particular case." *Id.* art. 59. Thus, there is no concept of stare decisis in cases before the ICJ.
- 15. Thus, international conventions are a more valuable source of international law than is international custom. See Rebecca M. M. Wallace, International Law 7-8 (1986); John W. Williams, Research Tips in International Law, 15 J. Int'l L. & Econ. 1, 7-10 (1981); Mark W. Janis, An Introduction to International Law 10-11 (3d ed. 1999).
- 16. International conventions are also referred to as treaties, pacts, accords and protocols, among other titles. *See* JANIS, *supra* note 15, at 9.

nations."¹⁷ The secondary means of determining international law include the "judicial decisions and the teachings of the most highly qualified publicists of the various nations."¹⁸ It is also important to remind students that the ICJ does not follow the concept of stare decisis as do domestic courts, so that the ICJ does not regard its own prior case law as binding precedent.¹⁹

A. Conventions

International conventions or treaties²⁰ are the sources students most easily comprehend, as students have heard of trea-

^{17.} ICJ Statute, *supra* note 10, art. 38(1)(c). The "civilized nations" language is *passé*. *See* JANIS, *supra* note 15, at 55; *infra* Part II.C.

^{18.} ICJ Statute, *supra* note 10, art. 38(1)(d). The term "most highly qualified publicists" refers to legal scholars. *See generally* BASIC DOCUMENTS IN INTERNATIONAL LAW (Ian Brownlie ed., 4th ed. 1995); WALLACE, *supra* note 15, at 25-26.

^{19.} Indeed, Article 59 of the Statute of the ICJ holds that "the decision of the Court has no binding force except between the parties and in respect of that particular case." ICJ Statute, *supra* note 10, art. 59. However, although they are not binding according to a strict interpretation of Article 38(1)(d), the court may follow its prior decisions under the doctrine of jurisprudence constante, whereby the court strives to render decisions that are "sequentially consistent." Janis, *supra* note 15, at 83. Thus, prior decisions of the court are still very persuasive.

^{20.} The best place to advise international law moot court students to begin a search for international conventions concluded since World War II is the United Nations Treaty Series ("U.N.T.S."). This series is the successor to the League of Nations Treaty Series ("L.N.T.S."), which contains a record of international conventions from 1920 to 1945. Although it is the most comprehensive collection of international conventions, the U.N.T.S. is far behind schedule in publishing the convention texts and indices. For information on how to properly use United Nations, United Nations Documentation: Re-SEARCH GUIDE, at http://www.un.org/depts/dhl/resguide/, see BRENDA BRIMMER ET AL., A GUIDE TO THE USE OF UNITED NATIONS DOCUMENTS (1962); WILLIAM H. PATCH, THE USE OF UNITED NATIONS DOCUMENTS (1962); and Publications of the United Nations System: A Reference Guide (Harry N. M. Winton ed., 1972). The American Society of International Law's International Legal Materials ("I.L.M.") is an excellent source of current international legal documents. Conventions are published bi-monthly in the I.L.M.. and some are published before they have entered into force. The U.S. government also publishes United States Treaties and Other International Agreements ("U.S.T."), which contains the bodies of conventions to which the United States is a party. Until 1950, U.S.-ratified treaties were also published in *Statutes at Large* and the I.L.M.

ties before, and they are most like a traditional domestic legal device – a contract.²¹ Just as a contract codifies the agreement of parties, a treaty memorializes the agreement between two or more states.²² International conventions bind both the states party to them, and those states that are not parties, but which nonetheless accept their provisions as law.²³ Parties to a con-

Other sources of current treaty information include Treaties in Force: A List of Treaties and Other International Agreements of the United States, which is published by the U.S. Department of State. This publication allows the researcher to determine quickly and efficiently what treaties the U.S. has entered into with other individual states. More current treaty information is published monthly by the Department of State in the Dispatch. Multilateral Treaties Deposited with the Secretary-General, which is published annually by the United Nations, allows the researcher to determine the parties to particular treaties, and the status of such treaties. Updated U.N. treaty information is published monthly in the United Nations Chronicle. Legal writing professors should encourage students to use these sources as they would use a digest to begin legal research in a domestic issue. Although they are not digests, these volumes contain similar subject indices which can help students to focus on the treaties that may be relevant to the particular issue they are researching.

- 21. In an attempt to help students understand the nature of treaties, it is useful to teach them that treaties are similar to two concepts with which they are familiar with contracts and statutes. Simply put, treaties are contracts between or among nations, and can be "interpreted" if necessary, by reference to their negotiating texts or *travaux preparatoires*, just like contracts can be interpreted by using parol evidence. In addition, just as we use cases to interpret statutes, we use cases, scholarly articles and treatises to interpret treaties.
- 22. RESTATEMENT OF THE LAW (THIRD) THE FOREIGN RELATIONS LAW OF THE UNITED STATES § 102(3) (1987) (International conventions create international law "when such agreements are intended for adherence by states generally and are in fact widely accepted.") [hereinafter Restatement].

Some scholars make a distinction between law-making treaties and treaties that are simply contracts. In general, a law-making treaty is one in which universal rules or rules of general application are set forth, and treaty-contracts are agreements between states that deal with a particular matter exclusively concerning them. Usually, only law-making treaties are a direct source of international law, because treaty-contracts create law only among the signatories. For further discussion of the distinction between the two types of treaties, see J.G. Starke, Starke's International Law 37-41 (I.A. Shearer ed., 11th ed. 1994), and Wallace, supra note 15, at 17.

23. Examples of such treaties include Vienna Convention on the Law of Treaties, May 23, 1969, 18 U.N.T.S. 232, 8 I.L.M. 679, U.N. Doc. A/CONF. 39/27 (1969); Vienna Convention on Diplomatic Relations and Optional Protocol on Disputes, Apr. 18, 1961, 23 U.S.T. 3227, 500 U.N.T.S. 95; Convention on the Prevention and Punishment of the Crime of Genocide, Dec. 9, 1948, 78

vention must abide by the terms of that instrument based on the principle of pacta sunt servanda, namely, that "[e]very treaty in force is binding upon the parties to it and must be performed by them in good faith."²⁴ According to Article 38(1) of the ICJ Statute, conventions may be "general or particular," meaning that they can be bilateral or multilateral, specific or comprehensive.²⁵ And, although a convention provides the strongest evidence of international law, a convention which seems to contradict or modify established international custom should be interpreted so as to best conform to established custom, rather than deviate from it, unless the convention was intended to change the existing custom.²⁶ International conventions can also be evidence of established international custom.²⁷

B. Customary International Law

International custom, or customary international law, is one of the most widely cited, and yet most elusive concepts found in international law. International custom must be distinguished from what is thought to be a state's "customary behavior." ²⁸

U.N.T.S. 277; and provisions of the U.N. Charter, June 26, 1945, 59 Stat. 1033.

- 24. Vienna Convention on the Law of Treaties, supra note 23, art. 26.
- 25. See Williams, supra note 15, at 7.
- 26. For further discussion on how to interpret conventions that conflict with generally accepted international custom, see Wallace, *supra* note 15, at 18-19, and Janis, *supra* note 15, at 11-40.
- 27. See Peter Malanczuk, Akehurst's Modern Introduction to International Law 40 (7th rev. ed. 1997). Malanczuk further claims that a researcher must be cautious when using treaties to infer what the rules of customary law are. See id. He argues that "treaties dealing with a particular subject matter may habitually contain a certain provision," but that provision is not necessarily representative of custom. Id. It is necessary to look to the intentions of the parties to the treaty and determine if they agreed upon that provision merely to codify the customary international law, or to distinguish it from customary law. See id. However, a treaty can be cited to as evidence of customary law "[i]f the treaty claims to be declaratory of customary law, or is intended to codify customary law." Id. If such a treaty is cited as evidence of customary law, it can be used against a state that was not even a party to the treaty, and thus is quite a powerful source of international law. See id.
- 28. Examples of practices followed by states include official governmental conduct such as statements, national court decisions and legislation on international matters. In *Research Tips in International Law*, Professor Williams states that customs are derived "from diplomatic practices between states,"

For a state's practice to become binding customary international law, the state must engage in the particular practice because it considers itself legally obligated to do so, rather than out of compassion, convenience or friendship. This sense of legal obligation to referred to as *opinio juris sive necessitatis* or simply, opinio juris.²⁹ Generally, a state must also engage in a particular practice for a significant period of time for that practice to be considered binding customary international law.³⁰

practices of international bodies where those practices are evidence of international attitudes, and the internationally accepted activities of domestic organs, such as the United States Supreme Court and various municipal legislatures." Williams, *supra* note 15, at 7-8.

29. Thus, the states must believe that non-compliance with the customary practice would produce legal consequences, such as sanctions. The term for such a feeling that a certain type of conduct is required by international law is *opinio juris sive necessitatis*. In discussing the doctrine of opinio juris in its *North Sea Continental Shelf* opinion, the ICJ stated:

Not only must the acts concerned amount to a settled practice, but they must also be such, or be carried out in such a way, as to be evidence of a belief that this practice is rendered obligatory by the existence of a rule of law requiring it. The need for such a belief, i.e., the existence of a subjective element, is implicit in the very notion of *opinio juris sive necessitatis*. The States concerned must therefore feel that they are conforming to what amounts to a legal obligation.

North Sea Continental Shelf (F.R.G. v. Den.; F.R.G. v. Neth.), 1969 I.C.J. 3, 44 (Feb. 20). It is unclear exactly how widely accepted a practice must be to meet the opinio juris requirement. In general, the custom must be such that it is accepted by the major world powers and the states affected by it, and not rejected by a large majority of states. *See* WALLACE, *supra* note 15, at 11-12.

Some states, such as the former Soviet Union, believed that only positive state action can be a source of international law, and thus, they argued that the only true primary source of international law is treaties. Williams, supra note 15, at 7. Williams says, "[t]he attitude of the Soviet Union toward international law is an example of positivism in practice. The Soviets have, in the past, consistently regarded treaties as the primary, if not the only source of international law." Id. For further discussion on this topic, see Janis, supra note 15, at 42-43; Welsley L. Gould, An Introduction to International Law 31-64 (1957); and G.I. Tunkin, Theory of International Law 89-203 (William E. Butler trans., 1974).

30. The United States Supreme Court held in *The Paquete Habana* that international law was created by "ancient usage among civilized nations . . . gradually ripening into a rule of international law." 175 U.S. 677, 686 (1900). The Court later described the time required for "ripening" as time "sufficient to have enabled what originally may have rested in custom or comity, courtesy or concession, to grow, by the general assent of civilized nations, into a settled rule of international law." *Id.* at 694. In the *Asylum Case*, the ICJ

Once a practice has become customary, and thus a recognized form of international law, all states that have not objected to the custom are bound by it.³¹

In addition to those practices recognized by states as customary international law, treaties between various states can also be evidence of international custom.³² Treaties often codify rules that states believe have become international custom through constant and uniform usage over a long period of time.³³ Evidence of international custom can thus be found by analyzing international conventions and other legal instruments, and determining how these instruments are interpreted and implemented by the various states.³⁴

C. General Principles of Law

The final primary source of international law is the "general principles of law recognized by civilized nations." Nowadays, the phrase "recognized by civilized nations" has virtually become obsolete, in recognition of the valuable contributions to international law by countries that may not, at some earlier time in history, have been considered "civilized" nations. The general principles of law is yet another difficult source for students to grasp because of the lack of a clear scholarly definition. In general, a legal principle becomes a binding general principle of law if states independently apply similar legal principles in a domestic setting. The theory is that if states independently apply these similar legal principles in settling

similarly held that customary rules must be based on "a constant and uniform usage." Asylum Case (Colom. v. Peru), 1950 I.C.J. 266, 277 (Nov. 20). However, Wallace argues that even if a state engages in a practice for only a short period of time, it does not necessarily mean that the practice does not qualify as international custom. Wallace, *supra* note 15, at 9. Wallace says, "[t]he fact that a practice has been engaged in only for a brief period of time will not in itself be a bar to the formation of a customary rule, provided that the other requirements of custom are met." *Id*.

- 31. See Janis, supra note 15, at 41-44.
- 32. See Malanczuk, supra note 27, at 40.
- 33. See supra note 30 and accompanying text.
- 34. The researcher can determine how the various states interpret and implement legal instruments by reading secondary sources, such as scholarly articles and treatises written on the particular subject matter under study.
 - 35. ICJ Statute, supra note 10, art. 38(1).
 - 36. See Janis, supra note 15, at 55.
 - 37. See id. at 55-59.

domestic matters, they impliedly consent to be bound by those legal principles on an international level.³⁸ For example, one may argue that if many countries initially permit circumstantial evidence to be admitted in judicial proceedings, this practice has been accepted as a general principle of international law. General principles are generally used as "gap filler" when there is no applicable treaty or customary law on a given issue.³⁹ This source of law is analogous to a United States state court using judicial decisions from other states because those decisions are not binding as precedent on the court, but have some persuasive value.⁴⁰ The best documentation of the general principles of international law are scholarly writings, treatises and legal encyclopedias.⁴¹

D. Secondary Means of Determining International Law: Judicial Decisions and Teachings of the "Most Highly Qualified Publicists"

The final means for determining international law are the "judicial decisions and the teachings of the most highly qualified publicists of the various nations."⁴² Just what is meant by secondary means, and how does this differ from conventions, custom and general principles, which are considered sources of international law?

In essence, the categorization of judicial decisions and scholarly writings as secondary means indicates that these two types of materials do not, in and of themselves, constitute

^{38.} Williams has defined the general principles of law as "general principles of justice, natural law, analogies to private law, principles of comparative law or general conceptions of international law." Williams, *supra* note 15, at 8. Examples of such domestic legal principles include equity, estoppel, pacta sunt servanda, unjust enrichment and the use of circumstantial evidence.

^{39. &}quot;General principles common to the major legal systems, even if not incorporated or reflected in customary law or international agreement, may be invoked as supplementary rules of international law where appropriate." RESTATEMENT, *supra* note 22, § 102(4).

^{40.} The general principles of law are generally used "to substantiate determinations of customary international law," or as "gap fillers" rather than as precedent. JANIS, *supra* note 15, at 5. *See also supra* Part II.B.

^{41.} See Williams, supra note 15, at 8, 33-321 (providing examples of primary and secondary sources in bibliographic note).

^{42.} *Id.* at 8 ("Judicial decisions include the decisions of both international and municipal courts.").

sources of international law.⁴³ Rather, we can *use* decisions and scholarly writings to determine whether concepts of customary international law or general principles exist.⁴⁴ For example, suppose a student wishes to argue that a treaty requires a country to act in a certain manner. The student may use the treaty text and negotiating texts to develop his or her argument.

Suppose, however, that the student wishes to argue that an international custom or a general principle requires a country to act a certain way. Because there is no single source that lists all of the customary international concepts or general principles, must the student (or international lawyer) research the practice of every nation or examine the legal systems of numerous nations? This would be a daunting, if not impossible task. Instead, however, the student could look to the secondary means – judicial and scholarly opinions – as evidence of either customary or general principles of international law. The international law moot court student, in fact, will often cite judicial and scholarly materials to develop and support a customary or general principles argument.

The international law moot court student must become comfortable with another way in which judicial decisions perform a different function in the international legal arena than they do in the American legal system. Although American courts acknowledge the precedential and persuasive value of court decisions, the ICJ does not follow the principle of stare decisis. The U.S. Supreme Court described the role of judges and scholars in creating international law in *The Paquete Habana*:

[We turn] to the customs and usages of civilized nations; and, as evidence of these, to the works of jurists and commentators, who by years of labor, research and experience, have made themselves peculiarly well acquainted with the subjects of which they treat. Such works are resorted to by judicial tribunals, not for the speculations of their authors concerning what the law ought to be, but for trustworthy evidence of what the law really is. 46

^{43.} STARKE, supra note 22, at 44.

^{44.} *Id*.

^{45.} See supra note 19 and accompanying text.

^{46. 175} U.S. at 700.

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Thus, the ICJ's function is to apply the law, not to make new law, and the works of publicists are a means of *ascertaining* the applicable law.⁴⁷ Researchers will use publicists' works and judicial decisions to interpret the various treaties and customs, and therefore define and argue points of relevant international law.⁴⁸

In short, because the sources of international law are usually unfamiliar to the first-year law student — who may at best be only somewhat confronted with American legal hierarchy—it is crucial to develop a curriculum that will introduce students to the basics of these concepts without overwhelming them with the complexities of international law that they would encounter in an upper level introductory public international law course.

III. INSTITUTION AND ADMINISTRATION OF AN ACADEMIC INTERNATIONAL LAW MOOT COURT PROGRAM

A. The Student Selection Process

Just as there are many students who will jump at the opportunity to study international law in the context of first-year legal writing, there will be many first-year students who have no interest whatsoever in this area, or who would rather hone their domestic research and writing skills during their introductory legal writing course. A look at the Villanova program shows how a first-year international law moot court program can be designed to meet the needs of interested students without preventing uninterested students from learning in a traditional domestic law format.

^{47.} According to Wallace, the works of publicists are "subsidiary means of determining what the law is on a particular issue at a particular point in time, and in the absence of any rule of *stare decisis* in international law, writings do not necessarily carry less weight than judicial decisions." WALLACE, *supra* note 15, at 25.

^{48.} Some general treatises on international law, written by highly qualified publicists, include J.L. Brierly, The Law of Nations: An Introduction to the International Law of Peace (Sir Humphrey Waldock ed., 6th ed. 1963); Ian Brownlie, Principles of Public International Law (5th ed. 1998); Janis, *supra* note 15; Malanczuk, *supra* note 27; 1 Oppenheim's International Law (Sir Robert Jennings & Sir Arthur Watts eds., 9th ed. 1992); and Starke, *supra* note 22.

During the 1994 spring term, Villanova first offered international law moot court to first-year students.⁴⁹ During the fall semester, after students had become accustomed to researching and writing traditional legal writing memoranda based on state or federal law, interested students attended a presentation on the international law moot court program. At that meeting, students were told about the basic differences between the traditional moot court class and the international law moot court option.⁵⁰ Because the course requires students to research sources of law substantially different from the traditional constitution-statute-case hierarchy covered during the first semester of law school, students were given the option to participate in the program or remain in a traditional moot court class that would address traditional domestic legal issues.⁵¹

Of course, if a law school happens to have an international law aficionado among the faculty members who teach first-year courses, the challenge of creating a first-year international law legal writing course might seem a natural outgrowth of that faculty member's academic interests. For those schools where the creation of such a program is desirable but not a natural outgrowth of the first-year faculty, there are a number of suggestions for creating and administering this type of program.

Under this kind of system, students may have a different legal writing professor for the second semester. Despite initial concerns about continuity and consistency of instruction, overall, students who opted to participate in the international law moot court program did not feel disadvantaged by switching professors at mid-year, nor did those students who switched into domestic law moot court legal writing sections.⁵²

^{49.} See DIANE PENNEYS EDELMAN, INTERNATIONAL LAW MOOT COURT COURSE SUPPLEMENT A-1 (2002) (on file with author).

^{50.} For example, in addition to differences in terminology, the students were told about the significant differences between domestic and international legal research and that participation in the international law moot court class would require attendance at additional class sessions.

^{51.} The program has been fully enrolled for every academic year.

^{52.} Syracuse, for example, divides its first-year students among several "law firms," including a "firm" that specializes in international law. See Telephone Message from Richard S. Risman, supra note 8. Syracuse solicits interest in the international law firm during the summer preceding the students' first-year, and selected students are exposed to international law

Selection of students for an optional international law moot court program can also work well at a school that operates, in whole or in part, on an adjunct system. In that situation, the school may hire one or more adjuncts who teach only during the semester when moot court is required.⁵³ Using a lottery system, the adjunct will "pull" interested students from the first-year class *without* sending students back into the other legal writing professors' class sections. Thus, the traditional legal writing professors and their students benefit because they have smaller moot court classes.

B. Course Materials

As mentioned previously, the field of international law is distinct from domestic law in its hierarchy of law, research materials and court procedures. Before those students enrolled in international law moot court can begin to research and draft writing assignments effectively, they must become familiar with the basic concepts and structures of international law. Toward that end, the professor should compile an international law supplement to the students' traditional legal writing test.⁵⁴ A useful supplement might include materials on practicing international law, structures of international courts and organizations and basic readings on the sources of international law. Additionally, the supplement would contain a list of web resources⁵⁵ and a variety of research and writing exercises.

Development of moot court problems is, of course, a crucial portion of designing a successful international law moot court course. One does not have to start from scratch, however. Since several law schools have instituted international law moot court programs, the opportunity to share problems makes problem development relatively painless. In addition, once a

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throughout the entire first-year legal writing program. *Id.* During the first semester, students work on international law problems arising from federal law, and during the second semester, they work on problems arising from treaty law. *Id.*

^{53.} Brooklyn Law School uses this system. Since 1984, Brooklyn Law School has hired one or more adjunct professors each spring to teach its international law moot court sections. *See* E-mail from Marilyn R. Walter, *supra* note 7.

^{54.} See infra Appendix A.

^{55.} See infra Appendix B.

class of first-year moot court students graduates, a problem may be modified and "recycled." Once a professor develops a successful problem, he or she may also modify it as the law changes over the years, i.e., if a relevant treaty is terminated or enters into force, or a new area of law (such as cyberlaw) emerges.

On a cautionary note, the international law moot court professor should avoid using or modifying previous Jessup or other official international law moot court competition problems in class. Not only may this raise copyright issues, but several of these competitions publish their best briefs on-line or in print, thus subverting the professor's ability to have the students research their problems independently and tempting students to plagiarize.⁵⁶

C. Supplemental Instruction

Mastering the basics of international law also requires additional class sessions. Students will discover that these sessions are valuable because they lay the informational foundation upon which they will build their working knowledge of international legal concepts and structures.

At the outset of the term, class discussions should focus on the nature of international law, including its sources, principle concepts and governing bodies. First, the professor should explain the sources of international law discussed above. Attention should focus on the hierarchical structure of the sources of international law and the weight placed on these sources by international institutions such as the ICJ.⁵⁷ Second, the pro-

^{56.} See generally ASS'N OF STUDENT AM. INT'L LAW SOC'Y, PHILIP C. JESSUP INT'L LAW MOOT COURT COMPETITION COMPENDIUM (2001). Published competition briefs, however, may provide examples of excellent briefs upon which students can model their work.

^{57.} One lesson to impress upon students is the difference between the precedential value of a U.S. Supreme Court decision in an American court as compared with a decision of an international court. In a domestic court, the existence of a Supreme Court decision would, of course, strongly influence the parties to a similar dispute in the state or federal courts. In an international court, however, a decision of the U.S. Supreme Court represents the viewpoint of only one country among many. See supra notes 14, 42-45 and accompanying text. See also, e.g., LaGrand Case (F.R.G. v. U.S.), 40 I.L.M. 1069 (June 27), available at http://www.icj-cij.org/icjwww/idocket/igus/igusframe. htm (last visited Feb. 19, 2002) (criticizing the United States Supreme

fessor should introduce students to the guiding principles of international law, such as jus cogens,⁵⁸ opinio juris,⁵⁹ and pacta sunt servanda.⁶⁰ Because these and other important international principles are unknown to new students of international law, they generally require a thorough explanation. Finally, it is important for students to understand the role played by international institutions such as the United Nations and the ICJ, two of the primary mechanisms for international dispute resolution. Once students begin to understand how these principles and institutions interact in the international arena, their research will progress much more effectively. There are numerous texts that can serve as a basis for discussing these and other international law concepts.⁶¹

Students exploring the field of international law for the first time are generally unfamiliar with the wide variety of resources available to the international law researcher. For most second-semester law students, familiarity with library resources is limited to domestic sources, such as case reporters, statutes, encyclopedias and digests. Although students may have been given a glimpse of international research materials during their first semester of law school, international research resources remain largely undiscovered to first-year students.

Before students delve into the research phase of their writing assignments, their legal writing professors should provide them with a general introduction to the variety of international law sources available both in print and electronically. Texts on legal research can provide students with the background necessary to begin a fruitful research process, 62 and on-line resources abound.63 After assigning these informational texts, professors should schedule a library tour so that the students can see first-hand the sources discussed in the texts. Interna-

Court's decision upholding the denial of the Vienna Convention on Consular Relations protections to foreign nationals convicted of a capital crime).

^{58.} See Vienna Convention on the Law of Treaties, supra note 23, art. 53.

^{59.} *See* Janis, *supra* note 15, at 46-48.

^{60.} See id. at 66.

^{61.} See generally Janis, supra note 15; Wallace, supra note 15; Williams, supra note 15.

^{62.} See Morris L. Cohen et al., How to Find the Law 451-95 (9th ed. 1989); Guide to International Legal Research (Geo. Wash. J. Int'l L. & Econ. ed., 2d. ed. 1993).

^{63.} See infra Appendix B.

tional and foreign law librarians can provide invaluable assistance conducting these tours and/or teaching the students how to perform international legal research.

A guided tour through the international sections of the school's law library will familiarize students with the wide variety of available international law resources. On a practical level, the tour acquaints students with the physical location of the resources and other tools, such as computerized databases, necessary to access the information. During the tour, a law librarian should briefly explain the type of information contained within each resource and how the students can effectively access the information. For general background information on international law, the law librarian should point out texts such as international treatises, encyclopedias and law journal articles.⁶⁴ Of particular importance to the students during the research phase of their writing assignments will be the international treaty collections, such as the *United Nations* Treaty Series, the League of Nations Treaty Series, the Consolidated Treaty Series and the Treaties and Other International Agreements Series. The law librarian should point out these and other valuable resources such as ICJ decisions, UN documents, and other organizational charters throughout the tour, and may introduce students to electronic resources as well.

The school's Jessup International Law Moot Court Team and any other international law moot court teams are other valuable resources that can provide students with additional background on the concepts and mechanics of international law. Mandatory attendance at an international law moot court team practice round, considered invaluable by Villanova students, 65 will assist students as they begin to formulate arguments for

^{64.} Prior to the tour, the professor might consider which types of documents will be particularly important to the students' research and should make sure the students are aware of these resources.

^{65.} This has been reported anecdotally by Villanova students over the past nine years. When surveyed about the value of attending oral argument at the 2002 Atlantic Regional Rounds of the Jessup Competition, which was hosted by Villanova, students overwhelmingly reported that observation of the arguments helped them to better understand the concept of customary international law, use and argument of international legal sources and advocacy in general. See Questionnaire for Students of Legal Writing, Section G at Villanova University School of Law, Villanova, Pa. (Feb. 12, 2002) (on file with author).

their writing assignment. Witnessing a practice round brings into focus elusive concepts such as customary international law and general principles of international law, which are often initially difficult for students to grasp. Actually hearing a participant explain customary international law to a judge during a practice round, for example, reinforces the information degested by students as they review introductory materials, begin their research and take part in classroom exercises. Finally, the team's practice round tends to quell feelings of anxiety experienced by students as they progress toward preparing for their own oral arguments. The practice introduces the students to the format of oral arguments and the types of questions they may be asked.

D. Classroom Exercises

While learning how to research international law, international law moot court students must also prepare to face the challenge of writing a formal, persuasive brief, which in international lingo is called a "memorial." Persuasive writing may come more naturally to some students than the rigid objectivity required in traditional first-semester legal writing On the other hand, many students are unfamiliar with the subtleties of persuasive writing and may therefore need some instruction. Regardless of their background, classroom exercises on the techniques of writing persuasive briefs are a useful tool to sharpen the skills of all studentswriting professors should design exercises that teach students the basics of constructing persuasive arguments. Again, the type and content of the exercises is limited only by the professor's imagination. In a typical exercise, the professor might provide the students with a packet of information that describes a hypothetical international legal dispute, a list of relevant international legal principles and sample memorial abstracts relating to the dispute. The professor should then divide the students into small collaboration groups, with each group representing a different country in the dispute, to help the students learn to identify international legal issues and the key facts and arguments that relate to them. The groups may

 $^{66.\ \, {\}rm Ted}\ \, {\rm T.}\ \, {\rm Amsden}\ \, \&\ \, {\rm Margaret}\ \, {\rm A}\ \, {\rm Costello},\ \, {\it Arguing}\ \, in\ \, the\ \, Hague,\ \, 73$ MICH. Bar J. 1094, 1094 (1994).

meet outside of class to discuss how the facts and international principles can be effectively molded into persuasive arguments for their side of the dispute. Students should come to the next class prepared to discuss their group's findings.

Questions for the students to consider might include: what facts do we emphasize to make our arguments more persuasive; what facts should we de-emphasize; and what international principles support our country's position? In addition, the students can draft different parts of their memorials — facts, summary of argument, point headings and the like — before completing a full draft of their memorials.

In-class discussion of the arguments formulated during collaborative, out-of-class sessions can develop into a lively debate as the students set forth persuasive arguments to further the interests of their assigned country. Discussion of the issues can focus on how the different groups chose to shape the facts in favor of their countries.

E. Citation Methods

An additional challenge confronted by students who choose to study international law is how to cite international legal materials properly. To prepare a thorough memorial, students typically will have to cite treaties, UN documents, decisions of international courts and tribunals and law review articles. Generally, during their first semester of law school, students learn only the basic rules of proper citation for domestic materials such as cases, statutes and law reviews. Therefore, students enter into the international law moot court program with little, if any, knowledge of how to cite international materials. As mentioned previously, there is a large body of international materials available to researchers, many with unfamiliar and often complicated citations. Spending some time reviewing the most commonly cited international materials, such as treaties, constitutions, statutes and UN documents aids students in their research and improves the accuracy of their citations. Citation forms for these types of materials can be found in both The ALWD Citation Manual: A Professional System of Citation⁶⁷ and The Bluebook: A Uniform System of Citation (com-

^{67.} Darby Dickerson & Ass'n of Legal Writing Dirs., The ALWD Citation Manual: A Professional System of Citation, R. 21.0 (2000).

monly known as the "Bluebook").⁶⁸ Either of these reference texts may be used to develop sets of legal citation problems to teach students how to cite previously unfamiliar international research materials.⁶⁹

IV. INTRODUCING INTERNATIONAL LAW INTO THE FIRST-SEMESTER LEGAL WRITING CURRICULUM

Granted, development and incorporation of a workable firstyear international law moot court program into the law school curriculum may require a bit of planning and a willingness to innovate in the first-year curriculum, but as shown above, "Where there's a will, there's a way." Incorporating international law into the first semester of the legal writing curriculum, however, is relatively simple.

During the first semester of a first-year legal writing course, students typically prepare a series of office memoranda based on hypothetical legal problems. Initial problems may use a "closed universe," that is, students are given a statute and/or several cases with which to analyze their client's problem and may not perform additional research. Subsequent problems usually involve "open" research, for which the student's research is only limited by parameters set by the professor.⁷⁰

So, why not internationalize the memo writing process by assigning problems that raise issues of international law? Consider these examples:

(1) Rule 44.1 of the Federal Rules of Civil Procedure regulates the method by which a party to litigation may raise an issue of foreign law in a federal court proceeding. The student must advise whether a client who wants the court to apply for-

^{68.} The Bluebook: A Uniform System of Citation R. 21, at 157 (Columbia Law Review Ass'n et al. eds., 17th ed. 2000).

^{69.} For example, professors should draft sample citations, which include a wide variety of sources, such as treaties, journals, arbitral awards, ICJ cases, treatises and UN documents, that are not in correct form. After the students complete the citations, provide them with the correct citation forms to ensure accuracy. These and similar exercises will make the task of citing international documents less daunting as students begin writing their research papers. While learning the new citation forms is challenging, students are generally pleased to broaden their knowledge with the variety of sources and the proper forms of citations.

^{70.} See Sourcebook, supra note 4, at 13.

eign law concerning the propriety of a foreign adoption can do so under the Rules.

- (2) The student represents a client that is a foreign corporation, which has been sued in federal district court. Under what circumstances can the client successfully move to dismiss the complaint based on forum non conveniens?
- (3) The client is a foreign resident who believes that a foreign bank may have illegally obtained assets stolen from her family during the Holocaust. Can she file suit under the California Code of Civil Procedure?
- (4) The client is party to a divorce proceeding pending in a foreign country. Can the foreign judge, magistrate or prosecutor obtain evidence from the client's U.S. bank to assist a foreign court in adjudicating the foreign proceeding under 28 U.S.C. § 1782?
- (5) The client was intentionally harmed by a national of a foreign country when the client was traveling abroad. If the tortfeasor travels to the U.S., can the court obtain jurisdiction over her under the Alien Tort Claims Statute?
- (6) A foreign government is considered by the United States to be a "state sponsor of terrorism." Can a U.S. citizen sue the foreign government successfully under an exception to the Foreign Sovereign Immunities Act?

These examples demonstrate but a few of the ways that the legal writing professor can internationalize the first semester of legal writing without requiring the students to analyze treaties, custom or other sources of international law. In fact, these problems illustrate the importance and role of international and foreign law in the American legal system. Through exposure to these issues, students can begin to see the importance of the actions and laws of foreign individuals and countries within our own legal system. A legal writing professor need not be an international law aficionado to incorporate international law into the first semester of the first-year legal writing program. All that is needed is knowledge of relevant domestic statutes and common law.

V. CONCLUSION

In the modern world made smaller by the Internet and instantaneous media reporting of world events, one can only assume that the interests of law students in matters of international and foreign law will not only grow, but familiarity with these concepts will be essential to their practice of law. The suggestions offered by this Article present curricular options that are relatively easy to incorporate into the first-year legal writing program. The opportunity to broaden our students' horizons can start when they enter the door to the law school. Why not seize this opportunity?

Is this experiment really worth the trouble? So far at Villanova, experience has answered this question with a resounding "yes." Despite being forewarned that participation in this program would require more difficult research and additional class hours, interest in the program has exceeded the number of class spaces available. Students who have completed the program have gone on to achieve membership on the *Villanova Law Review* and other law school organizations that base their selection criteria on either grades or completion of a substantial traditional legal writing project. In addition, students have found that their experiences have led to research assistant-ships involving international law, and have provided them with new conversation topics at job interviews.

In short, student experience has disproved the myth that a foray into a nontraditional subject during the first year of law school will somehow work to the students' detriment. Instead, the course has provided the students with a unique and challenging educational experience that broadens their world view while expanding the traditional first-year law school curriculum. Their experience should indeed prove that "[a] legal education that makes international norms an integral part of the program [should] enable us to view the world in a different way, and perhaps make us better able to function as lawyers and judges in a larger world."⁷²

^{71.} During a majority of the nine years since the inception of the Villanova program, there has been a waiting list for enrollment in the course. As of Spring 2002, more than 300 students will have taken part in the Villanova program.

^{72.} Jay M. Vogelson, *A Practitioner Looks at Globalization: II*, 46 J. Legal Educ. 315, 316 (1996).

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- Q. Case Concerning the Vienna Convention on Consular Relations, (Paraguay v. United States), Order dated April 9, 1998 and Declarations of President Schwebel, Judges Oda and Koroma

^{73.} This is an annotated copy of the Table of Contents from the author's International Law Moot Court Course Supplement for the Spring 2001 term. Diane Penneys Edelman, International Law Moot Court Course Supplement (2001) (on file with author). The problem used during that term involved the death penalty under international law, which is addressed in items P and Q on this table. Items A through D and J through M were prepared by the author. For more information, contact the author at edelman@law.villanova.edu.

APPENDIX B. INTERNATIONAL LAW WEB SITES

The list of international law web sites that are useful for research is virtually infinite. A sample follows:

- A. American Society of International Law Springboard http://www.asil.org/spgbd.htm
- B. American Society of International Law Program "Researching International Law on the Internet" http://www.asil.org/research.htm
- C. Cornell Law Library Legal Information Institute http://www.law.cornell.edu/world
- D. Global Legal Information Network, Law Library of Congress

http://www.loc.gov/law/guide/multi.html

- E. Hieros Gamos http://www.hg.org
- F. International Law Students Association Legal Links http://www.ilsa.org
- G. International Website Appendix, Professor William Slomanson, Thomas Jefferson School of Law http://home.att.net/~slomansonb/intlweb.html
- H. New England School of Law Center for International Law and Policy

http://www.nesl.edu/center

I. Syracuse University College of Law, Global Law & Practice Links

http://www.law.syr.edu/academics/academics.as what=global_links

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J. Villanova University School of Law, International and Foreign Law Finder

 $http://vls.law.vill.edu/compass/international/index. \\ htm$

INTERNATIONAL INVESTORS' RIGHTS AND REMEDIES IN THE ADJUDICATION OF DISPUTES WITH U.S. SECURITIES AND COMMODITIES FIRMS IN THE CONTEXT OF U.S. ARBITRAL FORUM SELECTION[†]

Madelaine Eppenstein*

I. Introduction

The globalization of markets, the internationalization, merger and consolidation of major investment firms, the join-der of commercial and investment banking and the interest of international public investors in utilizing the services of reputable, brand-name brokers, has contributed to a concomitant increase in customer claims filed in arbitration by both domestic and international investors. Yet, in practice, very few defrauded international investors who do business with United States securities and commodity futures firms through branch

[†] Copyright © 2002 Madelaine Eppenstein, New York, N.Y. Portions of this Article in substantially modified form were originally published by the author in *International Investors' Rights and Remedies in Regard to Fraudulent Investment Activities by U.S. Securities and Commodities Firms*, [Jan.-Dec.] 5 World Sec. L. Rep. (BNA), at 39 (May 1999).

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^{1.} See discussion infra note 18. Some of the increase in volume of case filings in 2001 was attributable to the bear market tech stock crash that began in the spring of 2000. See Richard Karp, Disputed Calls: A Year After Nasdaq's Peak, Arbitration Claims Against Brokers Soar, BARRON'S, May 21, 2001, at 21.

offices based both outside of and within the U.S., appear to be aware of their rights and remedies. Those who are savvy enough to discern that their boilerplate customer agreement with a securities broker-dealer or a commodities futures commission merchant ("FCM") usually requires adjudication of all claims in a U.S. based arbitral institution or reparations tribunal do not always, in the first instance, seek the advice of experienced U.S. counsel. Typically they will contact a member of this specialized bar in the U.S. only after first consulting their local counsel. Unless previously initiated to this area of practice, foreign counsel may advise their clients of potential claims in their own locality, but may be unaware of the investor's ability, if not the clear mandate under the broker's account-opening documentation, to obtain recovery through arbitration in the U.S.² Though international claimants may not

2. Under the Brussels Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters, "[t]he validity and enforceability of [alternative dispute resolution] clauses may be controversial, particularly if they contradict principles of consumer protection established by the Brussels Convention. Contract terms that deprive a consumer of the right to initiate legal proceedings in the Contract States where the consumer is domiciled are not likely to be enforced." Karol K. Deniston, Do Pre-Dispute Arbitration Agreements Violate Core Principles?, Paper Presented at the American Bar Association Section of Dispute Resolution Annual Conference (Apr. 27, 2001) (on file with Journal). See also Brussels Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters, arts. 2, 5, & 17, 1968 O.J. (C 27) 1, 4, 5, 8-9.

Another wrinkle suggested by Deniston may be presented by Article 7 of the Hague Conference on Private International Law, which currently provides that consumers can sue and be sued in the country where they are domiciled and can agree to the venue where a dispute will be adjudicated, but only if "such agreement is entered into after the dispute has arisen." Hague Conference on Private International Law, Preliminary Draft Convention on Jurisdiction and Foreign Judgments in Civil and Commercial Matters, at http://www.hcch.net/e/workprog/jdgm.html (Oct. 30, 1999); see also Deniston, supra note 2. Thus, as a general matter, typical U.S. broker-dealer predispute arbitration agreements, which prospectively waive access to the courts, may not be binding against the investor in the European Union. However, they are enforceable against the broker-dealer at the discretion of the international securities or commodity futures customer under applicable rules of U.S. self-regulatory organizations, based on the contract or the membership of the brokerage firm at the organization. See discussion infra note 12. Therefore, the practical applicability of these international norms in the context of regulated industries, such as the securities industry, may be a moot point.

be fully cognizant of the available legal rights and remedies, many intuitively recognize that, as the financial center of the U.S. and a global center for finance, as well as the site of the New York Stock Exchange, Inc. ("NYSE"), and the Nasdaq Stock Market, Inc. ("Nasdaq"), New York is the logical starting point to obtain legal advice.³

International customers who bring their claims under the auspices of the major self-regulatory organizations ("SROs") that run arbitration programs, such as the NYSE and the National Association of Securities Dealers Dispute Resolution, Inc. ("NASD-DR"), usually elect to have their disputes adjudicated in the U.S.⁴ New York City continues to be a magnet for

In recognition that our members and member organizations are expanding their businesses outside of the United States and increasingly offering their services to public non-institutional customers overseas, the Exchange will, where warranted by due process and fairness considerations, convene arbitration panels in London and Tokyo. Decisions on venue overseas will be made using the same criteria used domestically. Establishing these new hearing locations will accommodate non-U.S. customers of members or member crganizations in Europe and Asia who wish to avail themselves of the Exchange's arbitration facilities. In further recognition of this global expansion, members and member organizations doing business with public non-institutional customers outside of the United States, particularly in non-English speaking countries, must insure that the disclosures required by Rule 636 are communicated in a language in which the customer is fluent. Members and member organizations with public non-institutional customers outside the United States. particularly those doing business in non-English speaking countries, must conduct their own internal review of their accounts to insure that their Customer Account Agreements are in compliance with the required disclosure of the Arbitration Rules.

^{3.} See Carole Silver, Globalization and the U.S. Market in Legal Services-Shifting Identities, 31 LAW & POLY INTL BUS. 1093, 1135-36 (2000). The Nasdaq Stock Market, Inc., is currently an affiliate of the National Association of Securities Dealers, Inc., but is in the "process of becoming independent from the [National Association of Securities Dealers]" as part of a restructuring of the two companies, which will result in Nasdaq becoming an independent national securities exchange. Nasdaq Separates Further From NASD by Completing Share Repurchase, 34 Sec. Reg. & L. Rep. (BNA) No. 11, at 426 (Mar. 18, 2002).

^{4.} In only limited circumstances in a few locales will the SROs provide overseas venues. *See, e.g.*, Memorandum No. 98-42 from the New York Stock Exchange, to Members and Member Organizations (Dec. 15, 1998), *at* http://www.nyse.com/regulation/regulation.html. The memo states:

arbitration cases in general, as reflected in filing percentages.⁵ International investors who avail themselves of the advantages of U.S. based venue and counsel come from widely diverse economic backgrounds and geographic locations. In the author's practice, some of those who have successfully adjudicated disputes, through arbitration and mediation at the NYSE and NASD-DR, have included: a distant relation of a European royal family; an industrialist from Germany who was a majority shareholder in a company that conducted billions of dollars of global business a year; an international distributor of candy and confections from France; a dentist from Italy; representatives of a large Indonesian textile company; an investment company in Cyprus; a private investor from the Middle East; and a retired furniture manufacturer from Belgium. A common thread was that all of the investors brought claims of alleged wrongdoing in the business conduct of the overseas branch offices of large U.S. firms.⁶

^{5.} See discussion infra note 18. However, a breakdown of filings by domestic versus international claimants was not available from sources at the NYSE and NASD-DR. Generally, New York City venued cases account for 30-40% of the NYSE caseload. E-mail from Robert S. Clemente, Director of Arbitration, New York Stock Exchange, to Madelaine Eppenstein (Mar. 18, 2002) (on file with Journal). At NASD-DR, Northeast Region (comprised of offices across the Northeastern and Mid-Atlantic states, New York, Boston, Philadelphia, Pittsburgh, Albany, Buffalo, Baltimore, Norfolk and Richmond, as well as Washington, D.C.) venued cases were approximately 35% of their caseload, with cases centered in New York City comprising 18.3% of the entire region's caseload. Telephone Interview with Elizabeth R. Clancy, Associate Vice President and Regional Director Northeast Region, National Association of Security Dealers Dispute Resolution (Mar. 19, 2002).

^{6.} Each of these cases was settled during arbitration hearings or in mediation prior to the rendering of an arbitral award, with only one exception, a case that was on trial at the time this Article was written. As a result, the filings of these cases at an arbitral institution is not reflected in the database of the SROs awards. For a primary database online, NASD-DR works in conjunction with a service operated jointly by the Commerce Clearing House, Inc., securities and commodities law publisher, in partnership with the Securities Arbitration Commentator, Inc., a publication and database service based in Maplewood, New Jersey, as a way of providing a comprehensive, current, and publicly available database of annotated awards issued by a number of active forums such as NASD-DR, the NYSE, and the independent American Arbitration Association. See NASD Dispute Resolution, at http://www.nasdadr.com (last visited Mar. 6, 2002); Securities Arbitration Commentator, at http://www.sacarbitration.com (last visited Mar. 6, 2002).

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In each case, the international customer, and in almost all cases their local counsel, were unaware or unsure whether improper or fraudulent activity had caused the investment loss. Unfortunately, this phenomenon is widespread. It is also experienced by domestic public investors and has been reported often in U.S. court cases involving misrepresentation and concealed fraud. In the prosecution of the public customer cases mentioned above, it was only through diligent investigation and discovery, using procedural techniques developed through litigation in U.S. courts and at the SROs, that the nature of the wrongful conduct became apparent. Each of these international claimants recovered sizable amounts running into millions of dollars on average, sometimes well in excess of their out of pocket losses, through settlements achieved during or after the arbitration hearings (and before award), or in mediation.

While mediation may not have been widely employed in Europe until the end of the last century, except perhaps in the United Kingdom and Germany, "[a]rbitration has long been an accepted and even preferred method for solving international disputes." In practice, therefore, the potential claimant from

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^{7.} See, e.g., Fujisawa Pharm. Co. v. Kapoor, 115 F.3d 1332, 1335 (7th Cir. 1997); Law v. Medco Research, Inc., 113 F.3d 781, 786 (7th Cir. 1997); Marks v. CDW Computer Ctr., Inc., 122 F.3d 363, 367-69 (7th Cir. 1997); Nat. Rural Elec. Coop. Assoc. v. Breen Capital Serv. Corp., No. 00-722, 2001 WL 294086 (D.N.J. Mar. 28, 2001); Rotter v. Leahy, 93 F. Supp. 2d 487, 500-01 (S.D.N.Y. 2000); Dietrich v. Bauer, 76 F. Supp. 2d 312, 345 (S.D.N.Y. 1999); Morin v. Trupin, 809 F. Supp. 1081, 1097 (S.D.N.Y. 1993); Patsos v. First Albany Corp., 741 N.E.2d 841 (Mass. 2001). Frequently in such cases, the courts have held that the concealed fraud and misrepresentation effectively prevented the plaintiff from being put on inquiry notice of the wrongdoing, which sometimes operates to toll the applicable statutes of limitations.

^{8.} These procedural techniques include, but are not limited to: (1) sophisticated, database driven investigation of the rogue broker and the firm; (2) tracking down prior cases brought against the broker and the firm; (3) aggressively pursuing pre-hearing information and discovery requests and inperson pre-hearing conferences; and (4) early retention and involvement of the claimant's expert witness in initial client interviews and in rigorous analysis of account opening documents, the trading history and available records.

^{9.} Center for Public Resources, *Online Seminar, European ADR 2000: European ADR Practice, Issues and Trends* (Jan. 10-16, 2000), *available at* WL 18 ALTHCL 43. Arbitration as a method of resolving disputes that arise in international trade has a long history, and is conducted primarily in the

overseas may readily appreciate that arbitration of securities and commodities¹⁰ disputes is a viable, highly appropriate forum for the resolution of their claims.

This Article will focus on the practical considerations of potential claims and remedies available to the international customer in disputes arising against overseas offices of major U.S. broker-dealers and FCMs. Part II will provide the historical context in which the United States Supreme Court has mandated that claims arising under the U.S. securities laws are almost always subject to compulsory arbitration at the various arbitral self-regulatory organizations, where record filings by customers occurred in 2001.11 As demonstrated in Part III, under the commodities laws, however, there may be additional options, including court litigation and reparations. In either case, the international investor may seek the protection of both statutory and common law remedies in the U.S. to gain redress for fraudulent activity. Part IV addresses some recurrent scenarios that have given rise to various theories of liability for fraudulent conduct by a broker, and briefly touches on some common procedural considerations that may differ from systems of justice abroad. Concerns that are often expressed by the international investor when seeking to pursue claims in the

context of model laws enacted over the years to establish uniform standards for the settlement of international commercial disputes. See generally Vivienne M. Ashman, UNCITRAL Initiatives to Further Harmonize and Modernize Arbitration Laws, Rules and Practices, in INTERNATIONAL BUSINESS LITIGATION & ARBITRATION 2000, at 635 (PLI Litig. & Admin. Practice Course, Handbook Series No. 624, 2000) (citing Convention on the Recognition and Enforcement of Foreign Arbitral Awards, June 10, 1958, 21 U.S.T. 2518, 330 U.N.T.S. 38).

- 10. The commodity regulations require that public customers be given several options for filing claims, either in court, arbitration or before a reparations tribunal administered by the regulatory body that oversees the commodities markets, the Commodity Futures Trading Commission. See Commodity Exchange Act, 7 U.S.C. §§ 1-27 (2000) [hereinafter CEA]. See generally discussion infra Part III; Philip McBride Johnson & Thomas Lee Hazen, Commodities Regulation (2d ed. 1989); Philip McBride Johnson & Thomas Lee Hazen, Commodities Regulation (3d ed. 1998); Philip McBride Johnson & Thomas Lee Hazen, Special Supplement: Overview of the Commodity Futures Modernization Act of 2000 (3d ed. 2002).
- 11. See note 18 infra. For a general review of a wide range of topics covering the field of securities disputes, see Constantine N. Katsoris, *The Resolution of Securities Disputes*, 6 FORDHAM J. CORP. & FIN. L. 307 (2001) [hereinafter *The Resolution of Securities Disputes*].

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U.S. are addressed in Part V. But while these investors will likely face a number of fairly typical procedural and tactical issues, such as defenses based on statutes of limitations and so-called eligibility or timeliness rules at the SROs, along with preemptive, affirmative defenses and counterclaims asserted by the broker, the international investor ultimately has the opportunity to obtain a highly favorable recovery in an American court, arbitration or reparations proceeding.

II. CLAIMS FOR SECURITIES FRAUD AND RELATED CAUSES OF ACTION ARE CUSTOMARILY SUBJECT TO COMPULSORY ARBITRATION UNDER U.S. LAW

Until 1987, defrauded investors could choose to go to court and have a judge and jury decide their federal statutory claims under the U.S. securities laws. In the likely event that the defendant broker-dealer was a member of an SRO, such as the NYSE or the National Association of Securities Dealers, Inc., ("NASD"), claims in arbitration could be asserted upon the demand of the public customer, and access to the arbitral forum could be based on the membership provisions of those organizations even in the absence of an arbitration agreement.¹² Over-

12. Access to SRO arbitration based on membership of the respondent is still the rule. See N.Y. STOCK EXCH., art. XI, 2 N.Y. Stock Exch. Guide (CCH) ¶ 1501; N.Y. STOCK EXCH. R. 600(a), 2 N.Y. Stock Exch. Guide (CCH) ¶ 2600. Arbitration Rule 600(a) states:

Any dispute, claim or ontroversy between a customer or non-member and a member, allied member, member organization and/or associated person arising in connection with the business of such member, allied member, member organization and/or associated person in connection with his activities as an associated person shall be arbitrated under the Constitution and Rules of the New York Stock Exchange, Inc. as provided by any duly executed and enforceable written agreement or upon the demand of the customer or non-member.

Id. at R. 600(a). The NASD-DR provides similarly as follows:

Any dispute, claim, or controversy eligible for submission under the Rule 10100 Series between a customer and a member and/or associated person arising in connection with the business of such member or in connection with the activities of such associated persons shall be arbitrated under this Code, as provided by any duly whelmingly though, the choice for public customers was to go to court. But choice of forum was abrogated in 1987 by the Supreme Court in the seminal case of *Shearson/American Express, Inc. v. McMahon.*¹³ In that case, in which the author's firm represented the investors, the Supreme Court, by a close 5-4 vote, enforced the arbitration clause in a customer agreement pursuant to the Federal Arbitration Act ("FAA"),¹⁴ de-

executed and enforceable written agreement or upon the demand of the customer

NAT'L ASS'N OF SEC. DEALERS DISPUTE RESOLUTION, CODE OF ARBITRATION PROCEDURE R. 10301(a) (2001) [hereinafter NASD-DR ARBITRATION CODE].

13. 482 U.S. 220 (1987). *McMahon* was a dispute arising under the Securities Exchange Act of 1934, 15 U.S.C. §§ 78a-78mm (2000) [hereinafter 1934 Act]. Two years after deciding *McMahon*, in Rodriguez De Quijas *et al.* v. Shearson/American Express, Inc., 490 U.S. 477 (1989), the Court also relegated to arbitration claims arising under the Securities Act of 1933, 15 U.S.C. §§ 77a-77bbbb (2000) [hereinafter 1933 Act]. It is thus ironic that, in an area of virtually mandatory arbitration:

Securities disputes also generate a far higher proportion of judicial proceedings relating to arbitrability and interlocutory appeals than construction or other common types of arbitration Securities cases tend to dominate the case law of arbitration [T]he law of arbitration is being formed in the crucible of disputes between securities brokers and their customers.

Stephen K. Huber & E. Wendy Trachte-Huber, Top Ten Developments in Arbitration in the 1990s, 55 DISP. RESOL. J. 24, 34 (2001).

This phenomenon is not entirely inconsistent with the prediction, made by the late Justice Harry A. Blackmun, in his dissent in McMahon, that investors would be inclined to bring complaints in court regarding the results of mandatory arbitration. 482 U.S. at 267-68 ("[I]nvestors will be inclined, more than ever, to bring complaints to federal courts that arbitrators were partial or acted in 'manifest disregard' of the securities laws.") (citation omitted). If anything, for a time during the decade following McMahon, it was the industry that took the lead in resorting to the courts in an attempt to get judges, and not arbitrators, to micro-manage the arbitration process. See, e.g., Peter Blackman, No Clear Winner Yet: Brokerage Firms Seek to Derail Arbitration Effort, N.Y. L.J., Mar. 3, 1994, at 5. But see Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Driessens, N.Y. L.J., Oct. 24, 1996, at 27 (N.Y. Sup. Ct. Oct. 23, 1996). For a critical overview of the fallout in the arbitration process and the courts following the McMahon decision, see Constantine N. Katsoris, The Betrayal of McMahon, 24 FORDHAM INT'L L.J. 221 (1997); Constantine N. Katsoris, Riding the Trojan Horse Back to Wilko?, 10 SEC. ARB. COMMENTATOR 1 (1999).

14. Federal Arbitration Act, 9 U.S.C. §§ 1-307 (2000).

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spite historical aversion by both the courts¹⁵ and the Securities and Exchange Commission ("SEC") to the arbitration of securities fraud disputes.¹⁶ Since then, the caseload in arbitration has steadily increased.¹⁷ In 2000, for example, there were approximately 5,725 cases filed at the NASD, with a record

15. Prior to *McMahon*, every circuit court but two had adhered to a long-settled rule that pre-dispute arbitration agreements were unenforceable with respect to claims asserted under the 1934 Act. *See, e.g.*, Jacobson v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 797 F.2d 1197 (3d Cir. 1986); Mayaja, Inc. v. Bodkin, 803 F.2d 157 (5th Cir. 1986); Conover v. Dean Witter Reynolds, Inc., 794 F.2d 520 (9th Cir. 1986); Wolfe v. E.F. Hutton & Co., 800 F.2d 1032 (11th Cir. 1986); Mansbach v. Prescott, Ball & Turben, 598 F.2d 1017 (6th Cir. 1979); Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Moore, 590 F. 2d 823 (10th Cir. 1978); Weissbuch v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 558 F.2d 831 (7th Cir. 1977).

The Court of Appeals for the Fourth and District of Columbia Circuits had not appeared to have ruled per se on the question prior to *McMahon*. *See* King v. Drexel Burnham Lambert, Inc., 796 F.2d 59 (5th Cir. 1986); Miller v. Drexel Burnham Lambert, Inc., 791 F.2d 850 (11th Cir. 1986); Tashea v. Bache, Halsey, Stuart, Shields, Inc., 802 F.2d 1337 (11th Cir. 1986); DeLancie v. Birr, Wilson & Co., 648 F.2d 1255 (9th Cir. 1981); Ayres v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 538 F.2d 532 (3d Cir. 1976); Sibley v. Tandy Corp., 543 F.2d 540 (5th Cir. 1976). Included in this list is the decision of the Court of Appeals for the Second Circuit in favor of the investors below in *McMahon*, styled *McMahon* v. *Shearson/American Express, Inc.*, 788 F.2d 94 (2d Cir. 1986). The two exceptions were in the Court of Appeals for the First and Eighth Circuits. *See*, e.g., Page v. Moseley, Hallgarten, Estabrook & Weeden, Inc., 806 F.2d 291 (1st Cir. 1986); Phillips v. Merrill Lynch, Pierce, Fenner & Smith, 795 F.2d 1393 (8th Cir. 1986).

16. The stinging dissent of Justice Blackmun observed the contradiction in the SEC's support of the industry as an amicus in *McMahon*:

[U]ntil it filed an amicus brief in this case, the Commission consistently took the position that [section] 10(b) claims, like those under [section] 12(2), should not be sent to arbitration, that predispute arbitration agreements, where the investor was not advised of his right to a judicial forum, were misleading, and that the very regulatory oversight upon which the Commission now relies could not alone make securities industry arbitration adequate.

482 U.S. at 262. See also Exchange Act Release No. 19,813, [1982-1983 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,356, at 85,967 n.6 (May 26, 1983); Exchange Act Release No. 15,984, [1979 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 82,122, at 81,977-78 (July 2, 1979).

17. The steady rise in filings in customer arbitrations has historically been punctuated by peaks and valleys as a result of market driven or other forces, for example, the increase in filings following *McMahon*, which swept securities fraud cases under section 10b-5 of the 1934 Act into arbitration, the surge following the precipitous market break commonly known as "Black Monday" (Oct. 19, 1987), and the fall off in filings after the "crash" cases were

proximately 5,725 cases filed at the NASD, with a record 7,088 new claims filed in 2001.¹⁸ The NYSE, which historically has maintained a smaller caseload, had 780 filings in 2001.¹⁹

Arbitration generally at the NYSE and the NASD improved significantly after 1987 for the public customer, becoming more user-friendly. The Securities Industry Conference on Arbitration ("SICA"), "formed in 1977 to develop uniform rules governing the arbitration of disputes between broker-dealers and customers at [SROs]," and now comprised of three members of the public, representatives of seven SROs (including the NYSE and NASD-DR), and one voting representative of the Securities Industry Association ("SIA"), was responsible for preparing and adopting a Uniform Code of Arbitration ("Uniform Code") and making recommendations to improve the arbitration system at the SROs in a continuing process of review and evaluation of the operation of the Uniform Code and SRO arbitration.²⁰ The advent of enhanced arbitrator selection methods, which provide

resolved. See Sec. Indus. Conference on Arbitration, Eleventh Report of the Securities Industry Conference on Arbitration 106-26 (2001), available at http://www.nasdadr.com/pdf-text/sica_report.pdf (last visited Mar. 6, 2002) [hereinafter Eleventh Report].

18. Press Release, National Association of Securities Dealers Dispute Resolution, NASD Dispute Resolution Has Record Year (Jan. 22, 2002), available at http://www.nasdadr.com/news/pr2002/dr_release_02_001.html [hereinafter Press Release]. NASD-DR reported a 24% increase in filings in 2001 over the previous year's numbers, representing a record 2,137 claims filed in only the first four months of 2001, validating the notion that the tech stock decline in 2000 motivated the subsequent surge in customer complaints. Robust filings in the fourth quarter of 2001 did not appear to be affected by the tragic attacks on the World Trade Center in the heart of the financial center of New York on September 11, 2001. For updated filings and other statistics, see NASD Dispute Resolution, Dispute Resolution Statistics, at http://www.nasdadr.com/statistics.asp#grapha (last visited Mar. 5, 2002). NASD-DR recorded 20% more cases submitted to arbitration in the first two months of 2002 than the same period in 2001. Telephone Interview with Richard P. Ryder, Editor in Chief, Securities Arbitration Commentator (Mar. 22, 2002).

19. Statistics available from the Director of Arbitration at the NYSE. These claims include customer versus broker-dealer, broker-dealer versus customer and broker-dealer/employee cases.

20. Sec. Indus. Conference on Arbitration, Tenth Report of the Securities Industry Conference on Arbitration 1 (1998). See also Constantine N. Katsoris, SICA: The First Twenty Years, 23 Fordham Urb. L.J. 483, 535-38 (1996). See generally Thomas J. Stipanowich, Contract and Conflict Management, 2001 Wis. L. Rev. 831, 900 n.403 (2001).

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the parties with greater control of the process, clarification of procedures (generally for the appointment of arbitrators), initiation of continuing arbitrator training programs,²¹ expanded discovery options and the translation of the Uniform Code into plain English,²² provide the parties with a greater understanding and command of the process, providing them with greater input in choosing the arbitrators who will hear and determine their cases.²³ Liberalized rules facilitating the capture of information and document discovery well before the hearings on the merits are conducted improve the fairness of the process.²⁴ This is especially important in the case of the international public customer, who usually does not possess documentary proof or information concerning witnesses to fraudulent transactions and other wrongdoing, particularly when the latter

^{21.} Arbitrators are now required to undergo hours of training before they can sit on an arbitration panel, and must attend refresher training sessions to keep abreast of forum requirements and changes. See NAT'L ASS'N OF SEC. DEALERS DISPUTE RESOLUTION, ARBITRATOR RECRUITMENT BROCHURE (2000), available at http://www.nasdadr.com/arb_brochure_htm.asp (last visited Mar. 5, 2002).

^{22.} See ELEVENTH REPORT, supra note 17, at 5. The preface to The Arbitrator's Manual, compiled by SICA as a guide for arbitrators "designed to supplement and explain the [Uniform Code]," notes that "[s]ignificant differences between the Uniform Code and the procedures of the SROs," require arbitrators to "always consult the rules of the arbitration forum in which they are serving." Sec. Indus. Conference on Arbitration, The Arbitrator's Manual, pmbl. (2001), available at http://www.nasdadr.com/sica_manual.asp (last visited Mar. 6, 2002) [hereinafter Arbitrator's Manual].

^{23.} In cases where the damages alleged are over \$50,000, NASD-DR Rule 10308(b)(1)(B) provides for three arbitrators to sit on a case. See NASD-DR ARBITRATION CODE, R. 10308(b)(1)(B). NYSE Rule 607(a)(1) provides for a panel of three arbitrators where the matter in controversy exceeds \$10,000. N.Y. STOCK EXCH. R. 607(a)(1), 2 N.Y. Stock Exch. Guide (CCH) ¶ 2607. The method for selection of arbitrators is materially different at these two major SRO arbitral institutions, can be a complicated process and is a subject beyond the scope of this Article. See Theodore G. Eppenstein & Madelaine Eppenstein, Y2K Arbitrator Investigation and Selection, Paper Presented to the Public Investors Arbitration Bar Association Eighth Annual Conference (Oct. 20-22, 1999) (on file with Journal); Theodore G. Eppenstein & Madelaine Eppenstein, How to Select Arbitrators in Securities Arbitration, in Sec. Arb. 1996, at 585 (PLI Corp. L. & Practice Course, Handbook Series No. B4-7147, 1996).

^{24.} See NASD-DR Arbitration Code, R. 10321; N.Y. Stock Exch. R. 619, 2 N.Y. Stock Exch. Guide (CCH) \P 2619.

turn out to be internal employees of the broker-dealer or FCM and their overseas affiliated companies.

III. CLAIMANTS HAVE A RANGE OF OPTIONS WHEN PURSUING COMMODITY FUTURES CLAIMS

In the commodity futures area, investors typically use the services of introducing brokers ("IBs") who often act as investment advisors and utilize the services of FCMs in order to place orders in the commodity futures markets. The IBs are sometimes "guaranteed" by the FCMs pursuant to agreements entered into between the two. Investments can also be placed through associated persons of the FCM itself.²⁵ Fraud claims against commodity futures personnel may be brought against the FCM, the IB, their respective employees and Associate members. The claims can be based on theories of primary lability or aiding and abetting liability, as well as theories of agency and respondeat superior.²⁶

The IBs and FCMs also utilize customer agreements which are unlike those used by their securities industry counterparts. Pursuant to former Commodity Futures Trading Commission ("CFTC") Regulation section 180.3,²⁷ and the parallel amended section under the Commodity Futures Modernization Act of 2000 ("CFMA"),²⁸ when an IB or FCM wishes to place a predispute arbitration clause in its agreement with its public customer, in addition to the use of mandatory language, the customer is given more choices by statute than are available under the securities laws and regulations. To begin with, the predispute arbitration agreement must be accompanied by a separate arbitration clause and signature line. If the customer refuses to sign the separate arbitration clause, then the IB or

^{25.} See Nat'l Futures Ass'n, National Futures Association Manual ¶¶ 5011, 8101 (2001), available at http://www.nfa.futures.org/compliance/manual/index.html (last visited Feb. 23, 2002).

^{26.} CEA, 7 U.S.C. § 25 (2000) (affording a private right of action for violations of the CEA); 7 U.S.C. § 6b (prohibiting fraud, false reporting or deception); 7 U.S.C. § 13(c) (providing a private right of action for aiding and abetting liability); 7 U.S.C. § 2(a)(1)(A) (imposing agency/respondent superior liability).

^{27. 17} C.F.R. § 180.3 (2001).

^{28.} A New Regulatory Framework for Trading Facilities, Intermediaries, and Clearing Organizations, 66 Fed. Reg. 14262 (proposed Mar. 9, 2001) (to be codified at 17 C.F.R. pt. 166).

FCM must still honor the customer's wish to engage the IB or FCM, who cannot turn down a customer for failure to execute the pre-dispute arbitration clause.²⁹ Compare this with the typical securities industry account opening agreement involving credit with its customers, where, although pre-dispute language has become virtually universal and recited in bold print since *McMahon*, the broker-dealer can still insist that the investor sign the pre-dispute agreement as a pre-condition to doing business with the firm: the securities broker-dealer may refuse to accept the customer unless the customer agrees to the entire agreement.³⁰

There are as many as three fora to resolve commodity futures disputes: court, arbitration or reparations proceedings. The dispute resolution procedures offered under the Commodity Exchange Act ("CEA") are meant to be voluntary.³¹ They give

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This provision makes clear that the use of arbitration for the resolution of investor/broker-dealer disputes represents solely a choice of arbitration as a means of dispute resolution. Agreements cannot be used to curtail any rights that a party may otherwise have had in a judicial forum. If punitive damages or attorneys fees would be available under applicable law, then the agreement cannot limit parties' rights to request them, nor arbitrators' rights to award them. The agreements may not be used to shorten applicable statutes of limitation, restrict the situs of an arbitration hearing contrary to SRO rules, nor to limit SRO forums otherwise available to parties.

^{29. 17} C.F.R. §180.3.

^{30.} The SEC determined in 1988, following a study by a Commission staff of sixty-five broker-dealer firms that accounted for approximately 90% of all customer trading accounts in the U.S., that 96% of the margin accounts, 95% of the options accounts and 39% of the cash accounts at those firms at the time of the study were subject to pre-dispute arbitration clauses. SEC Self-Regulatory Organizations; Order Approving Proposed Rule Changes by the New York Stock Exchange, Inc., National Association of Securities Dealers, Inc., and the American Stock Exchange, Inc., Relating to the Arbitration Process and the Use of Predispute Arbitration Clauses, Exchange Act Release No. 26805, [1989 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,414, at 80,111-3 (May 10, 1989). However, despite the adhesive nature of the customer agreement, the SEC and the securities industry's primary SROs mandated in 1989 that the securities industry could no longer prevent public customers from asserting claims by contractually precluding punitive damages, shortening statutes of limitation, or otherwise cutting off statutorily mandated rights, as they had done previously. *Id.* The release further states:

^{31. 17} C.F.R. § 180.3(a).

the customer the right to forego arbitration and to file a claim in reparations, which is an administrative hearing before a U.S. administrative law judge.³² There is no jury trial in this proceeding. The customer can file a claim in reparations drectly, but is also given forty-five days in order to choose reparations after demand by the IB or FCM to arbitrate under a pre-dispute agreement, since the right to adjudication in reparations cannot be waived.³³ A potentially significant drawback for the international public customer, however, is that under 17 C.F.R. § 12.13(b)(4)(A) of the rules governing reparations, a nonresident of the U.S. must post a bond for double the amount of the claim.

This does not mean that customers cannot arbitrate at the National Futures Association ("NFA") against a member firm where there is no pre-dispute agreement. Claims have been prosecuted in arbitration at the NFA without a pre-dispute clause based solely upon the membership of the IB and FCM at the NFA.34 The NFA has its own arbitration rules,35 and is a registered futures association with oversight by the CFTC.³⁶ Commodity futures disputes can also be heard in arbitration at other alternative dispute resolution institutions, as a matter of contract law, if the organization is listed as an alternative forum in the pre-dispute arbitration agreement (or, as occurs only occasionally, the parties agree to arbitrate in a postdispute agreement), and under the proposed CFMA rules. The NYSE can also be a potential forum for commodities disputes when the respondent is a member of that exchange. However, although the NYSE's arbitration facility has been used successfully for major futures cases, according to the Director of Arbi-

^{32. § 180.3(}b)(3) ("The agreement may not require the customer to waive the right to seek reparations under section 14 of the [CEA, 7 U.S.C. § 18] . . . "). See also 17 C.F.R. § 12 (for the rules relating to reparations); McGough v. Bradford, 2000 CFTC Lexis 225 (C.F.T.C. Sept. 28, 2000).

^{33. § 180.3(}b)(3).

^{34.} NAT'L FUTURES ASS'N, CODE OF ARBITRATION ¶ 6017.1(a)(1)(i) (2001), available at http://www.nfa.futures.org (last visited Mar. 6, 2002) [hereinafter NFA CODE OF ARBITRATION]. This is similar to the rules in effect at the other SROs. See also supra note 12.

^{35.} NFA Code of Arbitration, ¶ 6011.

^{36.} CEA, 7 U.S.C. § 21 (2000).

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tration, relatively few of these have been filed at the NYSE.³⁷ Under similar circumstances involving membership, the NASD-DR may also be an appropriate forum.³⁸

Some FCMs, by design, omit the pre-dispute arbitration clause in their contracts. In fact, one major firm utilizes a clause which attempts to require customers, regardless of their domicile, to litigate all claims in the unlikely venue of a court sitting in Chicago. But NFA arbitral jurisdiction can be invoked by filing customer claims against members, despite such onerous clauses requiring court litigation in a distant or otherwise highly inconvenient venue. Where the customer is adequately represented it is possible to negotiate alternatives in such instances, and, for example, to obtain the mutual agreement of the parties to arbitrate the dispute under the auspices of an established futures arbitral institution such as the NFA.³⁹

No futures commission merchant . . . shall enter into any agreement or understanding with a customer in which the customer agrees, prior to the time the claim or grievance arises, to submit such claim or grievance to any settlement procedure except as follows: . . . (3) The agreement may not require the customer to waive the right to seek reparations under section 14 of the [CEA] and part 12 of these regulations.

17 C.F.R. § 180.3 (2000) (emphasis added). See also § 180.3-6 (mandated disclosures of non-waiveability of the right to bring a reparation case). The CFMA retains these protections under Section 2(a)(i) of the NFA CODE OF ARBITRATION, in which a customer has the absolute right to demand arbitration of a dispute with a member of the NFA. NFA CODE OF ARBITRATION, ¶ 6017.1. In one instance, a consolidation of separate cases on behalf of thirteen claimants, the parties entered into a stipulation that abrogated pre-dispute agreements to litigate in court in favor of the post-dispute stipulation to arbi-

^{37.} Telephone Interview with Robert S. Clemente, Director of Arbitration, New York Stock Exchange (Mar. 7, 2002).

^{38.} Under the proposed customer protection rules of the CFMA, claimants who choose to file claims in arbitration must be provided with a list of forum choices such as the contract market relating to the transactions at issue, a registered futures association, such as the NFA and at least one other "qualified" arbitral organization. A New Regulatory Framework for Trading Facilities, Intermediaries, and Clearing Organizations, 66 Fed. Reg. 14262 (proposed Mar. 9, 2001) (to be codified at 17 C.F.R. pt. 166). The NYSE and NASD-DR admittedly do not track the number of commodity futures cases which may have been filed there. See supra note 18; N.Y. STOCK EXCH. RR. 600(c), 635, 2 N.Y. Stock Exch. Guide (CCH) ¶¶ 2600, 2635. Such statistics were not available from the Directors of Arbitration. For court decisions and rulings of the CFTC, see, e.g., Comm. Fut. L. Rep. (CCH).

^{39.} Section 180.3 of the C.F.R. provides that:

IV. INTERNATIONAL INVESTORS ARE PROTECTED FROM AND MAY SEEK REDRESS FOR FRAUDULENT ACTIVITY

For the most part, the purchase and sale of securities are governed and regulated by the SEC⁴⁰ pursuant to the Securities Act of 1933 ("1933 Act")⁴¹ and the Securities Exchange Act of 1934 ("1934 Act").⁴² Both statutes have anti-fraud provisions, primarily under section 12(2) of the 1933 Act,⁴³ and under Rule 10b-5 of the 1934 Act, section 10(b).⁴⁴ Investors in the commodity futures markets can also seek redress for damages as the result of fraudulent activity under section 4(b) of the CEA.⁴⁵ Except in rare instances, however, individual investors cannot rely on the SEC, the CFTC or the SROs to prosecute their claims of fraud. Only through private civil court actions,

trate under the auspices of the NFA. See National Futures Association, Background Affiliation Status Information Center, at http://www.nfa.futures.org/bsic/details.asp?nfaid=001975&name=REFCO+LLC (last visited Mar. 5, 2002) (for arbitral awards).

The arbitration was also illustrative of the potential for complexity in resolving such cases: hearings on the merits commenced in fall 1998 and the case concluded with closing arguments in spring 2001; it involved the testimony of fifty-nine witnesses during 104 days of hearings, comprising over 24,000 pages of transcripts, in which over 400 exhibits were entered into evidence. *Id.* The arbitrators issued awards aggregating in total approximately \$43 million in damages. *Id. See also* Peter A. McKay & Ruth Simon, *Group of Investors Gets Award of \$43 Million*, Wall St. J., July 27, 2001, at C1.

- 40. The caveat to this general rule is that, while the SEC technically may have oversight authority over the arbitration process and rule changes thereof at the industry SROs pursuant to section 19 of the 1934 Act, as a practical matter, neither the SEC in the securities arena nor the CFTC in the futures industry has the ability to recover the claims of most public investors. 1934 Act § 19, 15 U.S.C. § 78s (2000). The attenuated exception is for commodities investor appeals from decisions in reparations proceedings against FCMs and other commodity professionals registered with the CFTC, which are adjudicated by administrative law judges or a CFTC hearing officer. A form of oversight may arise only because this process is administered by the CFTC, and subject to CFTC and U.S. federal court appellate review. See CEA, 7 U.S.C. § 18 (2000). See generally 13A JERRY W. MARKHAM, COMMODITIES REGULATION: FRAUD, MANIPULATION & OTHER CLAIMS § 20.01 (2000).
 - 41. 1933 Act, 15 U.S.C. §§ 77a-77mm (2000).
 - 42. 15 U.S.C. §§ 78a-78bbbb.
 - 43. 15 U.S.C. § 77*l*(2).
 - 44. 15 U.S.C. § 78j(b).
 - 45. 7 U.S.C. § 6b.

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arbitration, or reparations proceedings can both international and domestic customers seek compensation.

A. Theories of Liability

Claims against U.S. broker-dealers and FCMs, as well as their agents and employees, can be asserted under various theories of liability arising under statutory schemes and the common law. These include: (1) illegal trading where profitable trades and trades generating losses are shifted in and out of accounts of unsuspecting investors; (2) brokers who do not have written power of attorney engaging in unauthorized trading; (3) misrepresentations and omissions of material facts made by brokers in their recommendation of a purchase or sale; (4) brokers who fail to disclose the risks involved in a purchase or sale being recommended to the customer; and (5) market manipulation, to name a few.46 Depending upon the facts, other claims that may be asserted are: (1) claims of churning or excessive trading, which may include excessively high turnover in the account and trading effectively controlled by the broker for the purpose of generating commissions which are not in the customer's best interest, among other indicia; (2) unsuitable investments, which include investments recommended by a broker which are not in accordance with the customer's stated investment objectives or not in accordance with the customer's financial condition or tolerance for risk; (3) breach of fiduciary duty; (4) breach of contract; (5) negligence; (6) gross negligence; (7) misrepresentation; and (8) in certain limited instances, violations of the Racketeer Influenced and Corrupt Organizations Act ("RICO"),⁴⁷ among others.⁴⁸ Ancillary claims in support of primary fraud causes of action may be asserted in some cases: (1) for a firm's failure to properly supervise its salespersons; (2) violation of industry rules and regulations; (3) technical record

^{46.} See generally Markham, supra note 40, §§ 14-26; 3 Allan R. Bromberg & Lewis D. Lowenfels, Bromberg and Lowenfels on Securities Fraud & Commodities Fraud § 8 (2d ed. 2001) [hereinafter 3 Bromberg and Lowenfels].

^{47.} Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. §§ 1961-1968 (2000) [hereinafter RICO]. *See generally* JED S. RAKOFF, RICO: CIVIL AND CRIMINAL LAW AND STRATEGY § 7.04[2] (2000).

^{48.} See generally Markham, supra note 40, §§ 14-26; 3 Bromberg & Lowenfels, supra note 46.

keeping violations which may enable fraudulent activity; (4) violation of the firm's own policies, rules and regulations; and (5) failure to execute orders in a timely manner.⁴⁹

B. Procedural Considerations

As has been discussed previously, SRO arbitral institutions, such as exist at the NYSE, the NASD-DR and the NFA, administer their own rules of procedure and have great latitude in running arbitration hearings. For example, arbitrators are not technically required to follow the formal rules of evidence.⁵⁰ Thus, more testimony and documentary proof may be accepted into the record than in formal court proceedings. While the court system in the U.S. at both the state and federal level allows for appellate review, there are only limited grounds promulgated under the FAA, such as corruption by the arbitrators, and a limited, judicially created basis ("manifest disregard of the law") by which an arbitration award can be vacated or modified in a court proceeding.⁵¹

- 50. See, e.g., Arbitrator's Manual, supra note 22, at 29.
- 51. The FAA provides that an award may be vacated:
 - (1) where the award was procured by corruption, fraud or undue means.
 - (2) where there was evident partiality or corruption in the arbitrators. . . .
 - (3) where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced.

^{49.} See, e.g., In re GNP Commodities, Inc., [1992-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,360, at 39,214 (C.F.T.C. 1992), aff'd, Monieson v. Commodity Futures Trading Comm'n, 996 F.2d 852 (7th Cir. 1993) ("[F]ailing to place account numbers on order tickets does provide an opportunity to direct profitable fills to favored accounts, and [anti-fraud] section 4b of the CEA prohibits this type of allocation of winning and losing trades."). Under the securities laws and case law, there is virtually no private right of action for violation of stock exchange or other industry rules. However, these allegations are in practice almost always linked to viable primary claims such as statutory fraud violations, breach of fiduciary duty, breach of contract and negligence. See, e.g., 4 Allan R. Bromberg & Lewis D. Lowenfels, Bromberg and Lowenfels on Securities Fraud & Commodities Fraud § 15.06 (2d ed. 2001) [hereinafter 4 Bromberg & Lowenfels].

2002] INT'L INVESTOR REMEDIES

V. PROCEDURAL AND TACTICAL ISSUES FOR INTERNATIONAL CLAIMANTS

Some of the idiosyncrasies of the rules of practice in the U.S. may be unfamiliar to international claimants. Yet, invariably, and almost intuitively, these clients nevertheless raise questions about defenses they may be subject to, such as statutes of limitations, the potential duty to mitigate and the always popular defense based on the concept of "inquiry notice."

A. Statutes of Limitations and Eligibility Rules

Although both the CEA and the securities laws provide for private rights of action for claims of fraud,⁵² there are material differences in the statutes of limitations: two years from discovery of the fraud under the CEA⁵³ and one year from the discovery of the fraud, but no more than three from the accrual of the claim, under section 12(2) of the 1933 Act and section 10b of the 1934 Act.⁵⁴ There is generally an outside limit on the

(4) where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made.

Federal Arbitration Act, 9 U.S.C. § 10(a)(1)-(4) (2000). For the tension arising in the judicial interpretation of the "manifest disregard" non-statutory ground for setting aside awards, see, e.g., George Watts & Son, Inc. v. Tiffany & Co., 248 F.3d 577, 581 (7th Cir. 2001) ("[T]he 'manifest disregard' principle is limited to two possibilities; an arbitral order requiring the parties to violate the law . . . and an arbitral order that does not adhere to the legal principles specified by contract, and hence unenforceable under [section] (10)(a)(4).") (citing Eastern Associated Coal Corp. v. United Mine Workers of America, 531 U.S. 57, 62 (2000)). Cf. Halligan v. Piper Jaffrey, Inc., 148 F.3d 197, 204 (2d Cir. 1998) ("[W]here a reviewing court is inclined to find that arbitrators manifestly disregarded the law or the evidence and that an explanation, if given, would have strained credulity, the absence of explanation may reinforce the reviewing court's confidence that the arbitrators engaged in manifest disregard."). As discussed previously, following reparations proceedings in commodity cases, appeals are taken to a panel of CFTC commissioners and then to a federal circuit court of appeals.

- 52. See supra notes 43-45.
- 53. CEA, 7 U.S.C. § 25(c) (2000).
- 54. The affirmative defense of the statute of limitations, governed by a number of sections in the securities laws, including section 13 of the 1933 Act and sections 9(e), 19(c) and 29(b) of the 1934 Act, is too broad a topic for discussion here. It is important to note, however, that in 1991, the Supreme Court eliminated some of the complexity by holding that state borrowing provisions, which vary widely across the fifty plus U.S. jurisdictions, would

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ability to bring claims in SRO arbitration under the six year "eligibility" rule at the NYSE and the NASD, which, under the Uniform Code, "does not extend applicable statutes of limitation." The NFA has a meager two year timeliness rule, which tracks the two year statute of limitations under the CEA. The shorter two year NFA rule has the potential to create a serious conflict when state or federal statutory and common law claims of fraud, breach of fiduciary duty, breach of contract and others have longer statutes of limitations. ⁵⁷

no longer provide the basis for calculating statutes of limitations under the 1934 Act. See Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gilbertson, 501 U.S. 350 (1991). See generally Estate of Louis Loss & Joel Seligman, Fundamentals of Securities Regulation 1261-74 (4th ed. 2001).

55. The Resolution of Securities Disputes, supra note 11, at 324. NYSE Rule 603 also states:

No dispute, claim or controversy shall be eligible for submission to arbitration under this Code where six (6) years shall have elapsed from the occurrence or event giving rise to the act or the dispute, claim or controversy. This section shall not extend applicable statutes of limitations, nor shall it apply to any case which is directed to arbitration by a court of competent jurisdiction.

N.Y. STOCK Exch. R. 603, 2 N.Y. Stock Exch. Guide (CCH) \P 2603. The NASD-DR rule states essentially the same thing. NASD-DR Arbitration Code, \S 10304.

56. NFA Code of Arbitration, ¶ 6035, §5 & ¶ 6041, § 6(c). Section 5 states:

No Demand for Arbitration may be arbitrated under this Code unless a Demand or notice of intent to arbitrate . . . is received by NFA within two years from the date when the party filing the Demand for Arbitration knew or should have known of the act or transaction that is the subject of the controversy If, in the course of any arbitration, the Panel determines that the requirements of this section have not been met as to a particular claim, the Panel shall thereupon terminate the arbitration of the claim without decision or award.

Id. \P 6035, \S 5. Section 6(c) provides: "NFA shall reject any claim that is not timely filed, or for which the appropriate fee has not been paid." Id. \P 6041, \S 6(c). The CEA provides: "Any such action shall be brought not later than two years after the date the cause of action arises." 7 U.S.C. \S 25(c).

57. If a claim which may have already been accepted for adjudication by the NFA is found in the course of an arbitration to be ineligible ab initio under the NFA two-year rule, the panel of arbitrators has the authority to terminate that claim "without decision or award." NFA CODE OF ARBITRATION, ¶ 6035, § 5. Hypothetically, a claimant at the NFA can thus be placed in the untenable position (and the expense) of prosecuting a claim that was initially

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B. The Adversarial Nature of the Arbitration Procedure: Affirmative Defenses and Counterclaims

Not unlike litigation in general, arbitration claimants in æcurities and commodities disputes frequently grapple with novel issues and aggressive defense tactics. This is particularly evident in the securities context, in which an adverse award with written findings must be reported and usually ends up disclosed in the individual securities broker's Form U-4 or U-558 and Central Registration Depository ("CRD") reports.⁵⁹

accepted for adjudication by the forum, which may later be determined to be ineligible under the short two-year rule. Thus, diligence in timely filing claims is absolutely necessary. Some courts have determined that eligibility rules, as opposed to timeliness considerations, are not statutes of limitations, and issues arising under these time bars are matters for the courts, not the arbitrators, to decide. *See, e.g.*, Edward D. Jones & Co. v. Sorrells, 957 F.2d 509, 512-13 (7th Cir. 1992).

"A contrary line of authority leaves it to the arbitrators to deal with the six-year limitation period" generally regarding the limitation as procedural and a matter to be decided by the arbitrators. 4 BROMBERG & LOWENFELS, supra note 49, § 16.01(800). In New York, issues of timeliness, whether viewed as an eligibility rule or as a procedural statute of limitations, are in the province of the arbitrators and not the courts. See Smith Barney Shearson Inc. v. Sacharow, 689 N.E.2d 884, (N.Y. 1997); PaineWebber, Inc. v. Bybyk, 81 F.3d 1193, 1199 (2d Cir. 1996). As a result of an apparent conflict in the decisional law among the U.S. federal circuit courts concerning the complex issue of whether arbitrability matters are best decided by the courts or the arbitrators, the Supreme Court recently agreed to resolve the issue. See Dean Witter Reynolds, Inc. v. Howsam, 261 F.3d 956 (10th Cir. 2001), cert. granted, 70 U.S.L.W. 3385, 3530, 3533 (U.S. Feb. 25, 2002) (No. 01-800).

58. The U-4 is the form used for the required NASD registration of individuals associated with a brokerage firm, which itself must register with the NASD using registration Form BD. These forms also serve as the application for registration with the SEC. Exchange Act Release No. 31,660, [1992-1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,101 (Dec. 29, 1992). The Form U-5 is filed upon termination of registration. See NATL ASS'N SEC. DEALERS, NASD MANUAL & NOTICE TO MEMBERS §§ 3070-80 (2001), available at http://www.nasdr.com (last visited Mar. 6, 2002) [hereinafter NASD MANUAL AND NOTICE].

59. The CRD report is a publicly available filing maintained by the NASD which, among other things, lists a history of prior customer complaints against individual account executive registrants and broker-dealers. It is a highly useful tool for the investigation of the broker who is the subject of a customer claim. NASD Regulation, Inc., in its BROKER/DEALER FIRM USER'S MANUAL, defines the CRD report system as:

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Arbitration of these customer disputes, especially in large and complex cases, more nearly resembles court litigation than the simplified procedure that proponents of compulsory arbitration envisioned in the pre-McMahon era-a trend that is mirrored in international commercial arbitration. 60 In securities and commodity futures arbitrations, a claimant is likely to encounter the gamut of both affirmative defenses and preemptively asserted or baseless counterclaims, which often attempt to portray the investor as the culprit instead of as the victim. Such tactics, if played out in a U.S. court, might be subject to statutory sanctions. Examples include the assertion of groundless racketeering counterclaims, 61 a commonly asserted defense that tax motivated trading caused the customer's losses, and even the dubious defense of a major FCM alleging that a European customer, with no prior investment experience, somehow "knew" of the risks because she was warned by the account executive when opening the account that customers who manage their own funds only have about a 10% success rate in the fi-

[D]eveloped jointly by the [NASD] and the North American Securities Administrators Association . . . CRD was first launched in 1981 to centralize the registration process for the securities industry. . . . CRD made it possible to complete and send one application for an individual to be registered in all jurisdictions. . . . Over the past two (2) decades, the system has been expanded and modified extensively to meet the evolving needs of the NASD's constituencies. CRD currently maintains this information for more than half a million registered securities employees of member firms.

NASD REGULATION, BROKER/DEALER FIRM USER'S MANUAL 2 (2002), available at http://www.nasdr.com/webcrd_manual.asp (last visited Mar. 5, 2002). For publicly available information about NASD member firms and their associated persons, see NASD Regulation, NASD Regulation Public Disclosure Program, at http://www.nasdr.com/2001.asp (last visited Mar. 5, 2002).

- 60. See generally Christopher R. Drahozal, Commercial Norms, Commercial Codes, and International Commercial Arbitration, 33 Vand. J. Transnat'l L. 79, 96 (2000) ("Procedurally, international commercial arbitration is becoming more and more like public court litigation, particularly public court litigation as practiced in the United States.").
- 61. Note that securities fraud allegations based on predicate acts of mail and wire fraud under 18 U.S.C. §§ 1341, 1343, respectively, may no longer form the basis for a RICO claim or counterclaim, pursuant to the 1995 amendment to the RICO statute. RICO, 18 U.S.C. § 1964(c) (2000). See also Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, sec. 107, § 1964(c), 109 Stat. 737, 758 ("[N]o person may rely upon any conduct that would have been actionable as fraud in the purchase or sale of securities to establish a violation of [RICO] section 1962.").

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nancial futures marketplace.⁶² It is often the case that the foreign investor, mystified by, and with many questions concerning such tactics, should be introduced to the intricacies and challenges involved in winning a case of financial fraud. The following are just some of the more common defenses.

1. Defense of Contributory Negligence

The defense of contributory negligence is frequently asserted despite the fact that, under common law, contributory or comparative negligence are not defenses to intentional torts such as fraud.⁶³ Nor may contributory or comparative negligence arguments form a valid basis for a defense to fraud by the party who committed the fraud in cases alleging RICO violations.⁶⁴ In *Teamsters Local 282 Pension Trust Fund v. Angelos*, a securities case, the Court of Appeals for the Seventh Circuit emphasized that it would defeat the liquidity and efficiency of the markets to require a potential victim to take elaborate precautions against fraud, stating:

An ordinary investor is under no duty to investigate, though, and many people invest large sums in reliance on representations made to them or on the accuracy of the market price of the investment. The self-interest of those who seek to maintain reputations for honest dealing, and the legal rules against fraud, are the primary guarantors of the accuracy of representations in securities transactions. Investors are entitled to rely on these incentives to speak the truth and to recover damages from those who breach their duty to speak truthfully.⁶⁵

The same duty of care extends to commodity claimants. Under the CEA, courts have routinely held that a "customer does not have a duty to investigate the truth of the statements made

^{62.} If accurate, such a warning would have dissuaded any sane person from opening the account in the first place.

^{63.} See Greycas, Inc. v. Proud, 826 F.2d 1560, 1562 (7th Cir. 1987); City of New York v. Corwen, 565 N.Y.S.2d 457, 460 (N.Y. App. Div. 1990).

^{64.} Blue Cross and Blue Shield of New Jersey v. Phillip Morris, Inc., 36 F. Supp. 2d 560, 575-76 (E.D.N.Y. 1999); RESTATEMENT (SECOND) OF TORTS, § 545A (1977) ("One who justifiably relies upon a fraudulent misrepresentation is not barred from recovery by his contributory negligence in doing so.").

^{65.} Teamsters Local 282 Pension Trust Fund v. Angelos, 762 F.2d 522, 526 (7th Cir. 1985).

to him, but may ordinarily rely on the honesty of his account representative's representations."⁶⁶ As case law illustrates, the assertion of this defense is far from a guarantee that the respondent will prevail. Under New York law, and in most other jurisdictions in the U.S., the basic elements necessary to sustain a claim of fraud and misrepresentation sufficient to vitiate a respondent's risk disclosures are: (1) misrepresentation of a material fact; (2) the falsity of that misrepresentation; (3) scienter, or intent to defraud; (4) reasonable reliance on the misrepresentation; and (5) damage caused by such reliance.⁶⁷

In Indosuez Carr Futures, Inc. v. Commodity Futures Trading Commission, an account executive was less than candid in telling the customer that account statements should be disregarded because, even though they were inaccurate, that did not matter since the customer's non-discretionary account was hedged.⁶⁸ The Court of Appeals for the Seventh Circuit found that the customer's reliance was justifiable, since the "misrepresentations extended to the validity of the documents the mselves."69 In Commodity Futures Trading Commission v. Rosenberg, a broker's misrepresentations in reporting erroneous account balances and unlawful, unauthorized trading activity, for which the FCM was held vicariously liable, were deemed to "constitute information that a reasonable investor would consider important in trading commodity futures and options on futures," and were held to be in violation of the CEA.⁷⁰ The CFTC has opined that "[j]ustifiable reliance is not

^{66.} Jakobsen v. Merrill Lynch, Pierce, Fenner & Smith, Inc., [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22,812, at 31,393 (C.F.T.C. 1985). See also In re GNP Commodities, Inc., [1992-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,360 (C.F.T.C. 1992); Astor Chauffeured Limousine Co. v. Runnfeldt Inv. Corp., 910 F.2d 1540, 1550 (7th Cir. 1990) ("[A] liar may not lull the victim into a false sense of security and then say that the reliance was not justifiable.").

^{67.} See Granite Partners, L.P. v. Bear, Stearns & Co., Inc., 58 F. Supp. 2d 228, 257 (S.D.N.Y. 1999).

^{68.} Indosuez Carr Futures, Inc. v. Commodity Futures Trading Comm'n, [1992-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,125, at 41,718 (7th Cir. 1994).

^{69.} Id. at 41,723.

^{70.} Commodity Futures Trading Comm'n v. Rosenberg, 85 F. Supp. 2d 424, 447-48 (D.N.J. 2000) (citing Commodity Futures Trading Comm'n v. Skorupskas, 605 F. Supp. 923, 932-33 (E.D. Mich. 1985)) (finding issuance of false monthly statements constituted fraud in violation of the CEA).

a theory of contributory negligence, but rather is concerned with the causal connection between the misrepresentation and complainant's loss."⁷¹ Thus, a finding of non-reliance by a customer would necessarily imply that the customer "would have acted no differently had he known the truth."⁷²

2. Defense of Duty to Mitigate

The CFTC has held that "the duty to mitigate does not even arise in the context of fraudulent inducement" where there is no awareness by the customer of the material facts, and the broker has concealed his fraud.⁷³ This recognizes the fact that such customers are susceptible to being deceived by the false information: "Indeed, [the customer] was the victim of a fallacy that frequently affects the reasoning of investors—he allowed the accidental or random success of [the broker's] initial trading to confirm the false information conveyed to him concerning the ability of [the broker's] program to produce profit while controlling risk."⁷⁴ In this case, though the investor was the one who was duped by false representations, the CFTC deemed the FCM liable for its IB's duplicitous activity.⁷⁵

3. Defense of Ratification

Respondents may also allege that a claimant's actions are barred by the doctrine of ratification, and may also assert the related doctrines of waiver and estoppel, under the theory that the claims should fail as a matter of law because the claimant knowingly and voluntarily assented to them after they occurred. This defense is similar to that used by the defendant in *Karlen v. Ray E. Friedman & Co. Commodities*, in which the owners of a South Dakota cattle ranch sued their Chicago broker for unauthorized trading and churning.⁷⁶ The FCM based its defense on: (1) the plaintiffs' testimony that the bro-

^{71.} $\it Jakobsen, [1984-1986 Transfer Binder]$ Comm. Fut. L. Rep. (CCH) at 31,392 .

^{72.} Id.

^{73.} Levine v. Refco, Inc., [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) \P 24,488, at 36,116 (C.F.T.C. 1989).

^{74.} Id.

^{75.} Id.

^{76.} Karlen v. Ray E. Friedman & Co. Commodities, 688 F.2d 1193 (8th Cir. 1982).

ker plausibly convinced the customer, who called to object to unauthorized trades, that everything was in order; (2) the admission that the plaintiffs received confirmation slips for all trades and monthly activity statements; and (3) the fact that the plaintiffs "continued to invest substantial funds into their accounts even though [the broker] allegedly was disobeying their directions, and they were suffering significant losses."77 In *Karlen*, despite the alleged complacence of the plaintiffs, who were lulled by their broker into inaction, the Court of Appeals for the Eighth Circuit refused to accept the defense of ratification on the basis of the defendant's deception.⁷⁸ In affirming the plaintiffs' verdict below, the court squarely addressed the issue of ratification: "The question is not simply whether Karlen assented to the trades; rather it is whether his apparent assent was given voluntarily and intelligently with full knowledge of the facts."79 The court emphasized the complexity of the commodities markets and the confusing character of the materials provided by the broker, in which the statements sent to the plaintiffs did not include all trades and used confusing, technical language.80

Courts have thus declined to find ratification where an agent has acted fraudulently or in a manner designed to prevent customers from obtaining full knowledge of the trading activity. In another example, *Drexel Burnham Lambert Inc. v. Commodity Futures Trading Commission*, investors sued a wayward commodities broker for unauthorized trades.⁸¹ In affirming the CFTC decision against the broker, the Court of Appeals for the District of Columbia was steadfast in its support of the unwitting customers:

Circuit courts . . . have also deemed knowledge of the relevant facts and an intent to approve the unauthorized action after its occurrence to be preconditions to ratification.

... There is no evidence that [the customers were] aware that the checks they signed were to fund [the broker's] trading

^{77.} Id. at 1197-98.

^{78.} Id. at 1198.

^{79.} Id.

^{80.} Id. at 1198-1200.

^{81.} Drexel Burnham Lambert Inc. v. Commodity Futures Trading Comm'n, 850 F.2d 742 (D.C. Cir. 1988).

losses rather than the Treasury bill arbitrage program they were pursuing. 82

The confirmation reports and monthly statements which brokers usually rely upon to establish that somehow a claimant was able to determine the status of his accounts cannot be used for that purpose either, where a fraud has been committed against the investor. The *Karlen* court is again instructive:

Karlen's inability to determine the current status of the xcounts from the documents sent by Friedman is understandable. [The broker] executed a large number of trades in a short period of time, and Karlen had little experience in commodities to assist him in understanding the transactions. . . . Moreover, the plaintiffs were inundated with a large volume of documents of various types that had differing purposes which Friedman did not describe. Indeed, the documents used technical terms that did not plainly or precisely explain to an inexperienced or unsophisticated trader the information that they were providing. In fact, because the year-end and monthly activity statements sent by Friedman reported only closed transactions, they could convey seriously inaccurate impressions concerning the status of the accounts. For example, as the defendant concedes, the year-end statement for 1974 actually showed a \$1,000 profit, even though Karlen lost thousands of dollars that year when all outstanding contracts were finally closed. 83

The law is also clear that "[w]hen a customer lacks the skill or experience to interpret confirmation slips, monthly statements or other such documents" the broker is liable. As recognized by the Court of Appeals for the Eighth Circuit in *Karlen*, as well as by other courts, the duty lies with the broker:

[C]onfirmation slips and monthly statements do not enable a customer to determine his or her overall position or the total amount of real profit or loss occurring, unless the customer is sufficiently skilled to elaborate upon them to make that de-

^{82.} *Id.* at 750. *See also* Lazzaro v. Manber, 701 F. Supp. 353, 363 (E.D.N.Y. 1988) (deeming defendants' claim of ratification insufficient to dismiss a 10b-5 securities fraud action where investors claimed they lacked full knowledge and were unaware of risks due to manipulations and misrepresentations).

^{83.} Karlen, 688 F.2d at 1200.

^{84.} *Id*.

termination. . . . courts have generally refused to find that they relieve a broker of liability for its misconduct. 85

4. The "Boilerplate" on the Back of a Broker's Statements, in Confirmations, and in Customer Agreements, Do Not Give Rise to a Valid Ratification Defense

In *Karlen*, the circuit court rejected a typical ratification defense, based on its lengthy examination of the confirmations and monthly statements, including the pro forma legend on the back of the broker's documents:

Friedman confirmed each trade by mailing the plaintiffs, on the morning after the trade, a written confirmation slip describing the type, price and quantity of the commodity traded. In addition, each month Friedman mailed to the plaintiffs an activity statement which reported trades executed during the preceding month, the net profit or loss on transactions that were closed that month, and an account balance reflecting the closed transactions. Each monthly activity statement was accompanied by a document entitled "Statement of Account-Open Trades." These documents reported under the column title "open trade equity," the profit or loss that would have been recognized on all open contracts if they had been closed on the final day included in the monthly statements. The phrase "open trade equity" was not defined or explained in the "Statement of Account-Open Trades" document. Finally, Friedman, from time to time, mailed documents entitled "Statement of Account-Purchase and Sale." Although the purpose of these forms was not described in the record, they were apparently sent when the plaintiffs either deposited funds or closed out their position in any futures contract. All of the documents mailed by the defendant included the name, address and telephone number of Friedman, and contained the legend: "NOTE: PLEASE REPORT ANY DIFFERENCES **IMMEDIATELY.**"86

Numerous other cases have also held that the exculpatory effect of a pro forma risk disclosure statement will be vitiated where the risks of trading are undisclosed or misrepresented.⁸⁷

^{85.} Id. (citations omitted).

^{86.} Id. at n.7.

^{87.} See, e.g., Oram v. Nat'l Monetary Fund, [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,670 (C.F.T.C. 1987) (risk disclosure not

In *Reed v. Sage Group, Inc.*, the CFTC held that standard risk disclosures are a mere formality, and that boilerplate risk disclosure cannot cure false information and misrepresentations.⁸⁸ Depending on the relationship between the customer and broker, such as cases in which accounts are discretionary, fiduciary obligations may be viewed as more expansive, obligating the broker to disclose *more* than what appears in the standard risk disclosure statement. In *Hannay v. First Commodity Corp.*, the CFTC held that risk disclosures are not dispositive and do not vitiate misrepresentations: "We repeatedly have held that conduct can vitiate the effect of the risk disclosure statement mandated by our rules." ⁸⁹

5. Additional Considerations Regarding the Arbitration Process

There are a few other important issues that should be of interest to the international claimant. Securities and commodity futures cases often arise from dealing with SRO member firms that have overseas offices, where international customers may be more conversant than U.S. citizens with financial futures, different currencies and exchange rates. Consistent with the case law cited previously, this does not permit the inference that non-U.S. citizens are sophisticated investors solely on the basis of their familiarity with currency exchange or their conduct of transnational business. Indeed, broker conduct at international branch offices of U.S. brokerdealers can suffer from poor supervision and, as a consequence, brokers at these branches may be more inclined to dispense with following the firm's policies, rules and regulations, even though they are still subject to U.S. law and exchange rules and regulations.

dispositive of reliance where misrepresentations were claimed); Hannay v. First Commodity Corp., [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,936 (C.F.T.C. 1987) (claims of profitability vitiate effect of risk disclosure statement); Miller v. First Commodity Corp., [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,215, at 32,586 (C.F.T.C. 1986) (Exaggerated predictions of "virtually unattainable rate of return" are not negated by risk disclosure statement.).

^{88.} Reed v. Sage Group, Inc., [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,943, at 34,304 (C.F.T.C. 1987).

^{89.} *Hannay*, [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) at 34,282.

Claimant's counsel usually require expert assistance to understand the intricacies of the markets and how particular products work, and to assist in prosecuting cases either in arbitration, reparations proceedings or in court. More than one expert may be necessary to testify for the claimant in the larger damage case in which, aside from requiring expert testimony on damage theories and calculations, there are back office and supervisory issues, and specific defenses that call for the experience and knowledge of qualified experts who have practiced in the field.

In the event that claimant's counsel deems it necessary to pursue the testimony of former employees of the brokerage firm, there may be some obstacles to obtaining the presence of witnesses domiciled outside the venue of the arbitration forum or outside the U.S.⁹⁰ However, as current account executives and supervisors of foreign branch offices are presumptively registered individuals at the NYSE, NASD, or both, they are required by the forum to appear as a consequence of their registration status.⁹¹ If such individuals are sued personally, jurisdiction usually attaches even though they may have left the industry for several years. The same rule applies with respect to CFTC and NFA registrants.⁹² Similarly, if witnesses are still employed by the firm being sued, even if the witnesses are not registered, they will have to abide by a request from the arbitration panel to appear and testify. Resort should be made to the rules of the forum in which the case is pending and the appropriate jurisdiction from which subpoenas can be issued in order to have the ability to call all the important witnesses to testify.93

Arbitration is a private matter. As opposed to court proceedings, arbitration cases are held behind closed doors and are not open to the public. Because of the private nature of the process, confidentiality agreements are commonplace with respect

^{90.} See generally FED. R. CIV. P. 45; 28 U.S.C. § 1783 (2000) (covering service of subpoenas directed to a witness present in the U.S. or in a foreign country, who is a national or resident of the U.S., respectively).

^{91.} See sources and text cited supra note 12.

^{92.} See NFA CODE OF ARBITRATION ¶ 6017.1(a)(1)(i). On retention of jurisdiction, see, e.g., NASD MANUAL AND NOTICE, supra note 58, art. III, § 6, art. IV, § 4 & art. V, § 4.

^{93.} See Fed. R. Civ. P. 45; 28 U.S.C. § 1783.

to information and documents exchanged by the parties and exhibits entered into evidence at the hearings. When cases are settled prior to an award being rendered by the arbitration panel, the settlements usually contain confidentiality provisions. Arbitration awards, however, are made publicly available by the NASD-DR, NYSE and NFA.⁹⁴

Smaller cases can usually be arbitrated in several days, but the large and complex cases take many days, if not months, to hear. It is not unusual for cases of this genre to stretch out for a period of two to three years, in part because arbitrators have other pursuits, but, unlike judges, they do not sit on a case from day to day until concluded, and may only set aside two or three days a month to conduct hearings. Likewise, the attorneys for the parties may have other trial commitments that make adjournments and delays inevitable.

In almost all cases, preliminary hearings, also known as "initial pre-hearing conferences," are advisable so that the arbitrators can resolve discovery disputes between the parties and other pre-trial matters. ⁹⁵ But, discovery in arbitration is relatively limited compared with discovery obtainable in a court proceeding, especially when arbitrators are inclined to interpret requests narrowly; however, counsel usually can prevail by drafting comprehensive demands and requesting rulings when those demands are unfulfilled. In court, each party can take pre-trial depositions, proceedings in which statements from witnesses and parties are taken under oath and documents are produced. Non-party witnesses are also subject to depositions. Deposition discovery not only lengthens the time period of court litigation but also adds to the cost of the proceedings. These are two fundamental reasons why, except under extraordinary circumstances, depositions are usually not permitted in arbitration.

^{94.} NASD-DR awards are available online on its website, http://www.nasdadr.com, and are required to be made publicly available. See NASD-DR Arbitration Code, R. 10330(f). NYSE awards are accessible online at http://www.nyse.com/arbitration/decisions. The NFA provides summary awards online at http://www.nfa.futures.org/basic (access requires knowledge of the name of the broker or case identification number). Most are available through Securities Arbitration Commentator, Inc., at http://www.sacarbitration.com.

^{95.} See NASD-DR Arbitration Code, R. 10321(d)(1); N.Y. Stock Exch. R. 619(d)(1), 2 N.Y. Stock Exch. Guide (CCH) ¶ 2619.

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The arbitrators at the SROs, by regulation, must render an award within thirty days of the close of the proceedings and record, unless otherwise provided.⁹⁶ An additional advantage of SRO arbitration is that members must pay arbitration awards promptly or be subject to regulatory sanction and possible suspension of their licenses to operate.⁹⁷

VI. CONCLUSION

Many international investors have an opportunity to obtain damage awards in the U.S. either through cases brought in arbitration, court or reparations proceedings. For any aggrieved investor, it is advisable to investigate claims thoroughly prior to initiating proceedings, since a great deal of time and expense can be expended before and at the hearings, and it is essential to explore whether one has a solid case before such a commitment is made. Although the rights and remedies of investors are primarily governed by statute and within the customer agreement, the foreign branch offices of U.S. brokerdealers and FCMs are subject to arbitration procedures based

96. See NASD-DR Arbitration Code, R. 10330(h); NASD Manual & Notice, supra note 58, art. VII, § 3; N.Y. Stock Exch. R. 627(d), 2 N.Y. Stock Exch. Guide (CCH) ¶ 2627; NFA Code of Arbitration, ¶ 6059.7(g), § 10.

97. See NASD-DR ARBITRATION CODE, R. 10330(h); NASD MANUAL & NOTICE, supra note 58, art. VI, § 3; N.Y. STOCK EXCH. R. 627(g), 2 N.Y. Stock Exch. Guide (CCH) ¶ 2627; NFA CODE OF ARBITRATION, ¶ 6059.7(g), § 10. While motions (or petitions) to vacate arbitration awards are rarely granted, the NASD-DR has promulgated regulations governing the requirement that awards be paid to the customer within thirty days following the granting of a motion (or petition) to affirm the award in court. The relevant section providing for sanctions for noncompliance states:

The NASD after 15 days notice in writing, may suspend or cancel the membership of any member or the registration of any person in arrears in the payment of any fees, dues, assessments, or other charges or for failure to furnish any information or reports requested pursuant to Section 2, or for failure to comply with an award of arbitrators properly rendered pursuant to the Rules of the Association, where a timely motion to vacate or modify such award has not been made pursuant to applicable law or where such a motion has been denied, or for failure to comply with a written and executed settlement agreement obtained in connection with an arbitration or mediation submitted for disposition pursuant to the Rules of the Association.

NASD Manual and Notice, supra note 58, art. VI, § 3. See also sources and text cited supra note 51.

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upon the membership of those firms at SROs, such as the NYSE, NASD-DR and the NFA. In all cases, individuals and companies who have been unfairly treated should consult professionals who are knowledgeable in this area for a review of their rights and remedies.

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ONE COUNTRY, TWO SYSTEMS: THE INHERENT CONFLICT BETWEEN CHINA'S COMMUNIST POLITICS AND CAPITALIST SECURITIES MARKET

William I. Friedman*

I. INTRODUCTION

The Communist Party ("Party") took control of China following the country's 1949 Revolution.¹ This new government implemented a centrally controlled economic system, by way of abolishing free markets and nationalizing the nation's private companies into state-owned enterprises.² The Chinese Marxists theorized that this type of planned economy would result in maximum productivity and efficiency, since the entire population would be employed for the good of the country.³ However, contrary to these Marxist beliefs, this state-run economy produced few incentives for its people to pursue operational efficiency, and no accountability for the profits or losses of their businesses.⁴ As a result, the Chinese economy generated massive waste and losses.⁵

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^{1.} K. Matthew Wong, Securities Regulations in China and Their Corporate Finance Implications On State Enterprise Reform, 65 FORDHAM L. REV. 1221, 1221 (1996).

^{2.} See id.

^{3.} See id.

^{4.} See id.

^{5.} See id.

While the state sector was ailing, the private sector was doing very well, as it generated a large influx of profits and savings. Hence, an overwhelming majority of the capital in China was in the hands of the populous.⁶ The government viewed the disparity in wealth between the state-owned sector and the private sector as politically threatening. Similar to that of the Soviet Union's communist government in the 1980's, China was starting to feel the pains of its ailing economy, as its stateowned enterprises were on the brink of dissolution and bankruptcy, and therefore in serious need of capital. Thus, in 1978, the leading senior official in China, Deng Xiaoping, adopted an "open door" policy, centering on economic reforms utilizing market mechanisms and foreign resources to speed up the growth and modernization of the economy. Deng characterized his new open door policy as "socialism with Chinese characteristics."8

In pursuing this economic reform, the Party put into effect a strategy of "corporatization" (the conversion of state-owned enterprises into shareholding companies) and "securitization" (the sale of shares of state-owned enterprises in the securities market)⁹ with "limited privatization" (minority private equity participation in state-owned enterprises so as to enable the government to retain majority control of the market).¹⁰ These governmental strategies were implemented with the intention of coaxing the private sector into investing its capital into the Chinese securities market, which was still susceptible to state

^{6.} See C. Lan Cao, Chinese Privatization: Between Plan and Market, 63 Law & Contemp. Probs. 13, 43-44 (2000) ("Over the years, the prosperity of the non-state sector allowed China's private citizens to save large amounts of money. With one of the highest annual savings rates in the world – approximately thirty percent – private surplus capital at one point constituted approximately 1.3 trillion yuan or \$260 billion, although other sources put the amount at \$310 billion, with an estimated \$200 billion idle in the domestic banking system and another \$100 billion concealed outside the system, under mattresses.").

^{7.} Todd Kennith Ramsey, China: Socialism Embraces Capitalism? An Oxymoron for the Turn of the Century: A Study of the Restructuring of the Securities Markets and Banking Industry in the People's Republic of China in an Effort to Increase Investment Capital, 20 Hous. J. Int'l L. 451, 456 (1998).

^{8.} Wong, supra note 1, at 1221.

^{9.} Cao, *supra* note 6, at 14, 43-44.

^{10.} Ramsey, supra note 7, at 462-63.

control.¹¹ As a result, the government was able to tap into a large pool of private capital in the non-state sector, which has since been used to revitalize the financial self-sufficiency and solvency of China's state-owned enterprises and promote the country's socialist economic plan.¹² The development of a securities market has also had the effect of attracting a capital infusion from the international community, as China has become second only to the United States in terms of foreign direct investment inflows.¹³ Moreover, it has had the effect of steering money from the private sector toward investment rather than consumer spending, which has cooled down a possibly overheated, inflationary economy.¹⁴

As a result of its reform program, China has produced an economy with one of the most rapid growth rates in the world. This growth is largely attributable to the fact that China has lessened its stranglehold over its industries, as it has allowed them to be driven more by market forces and less by state directives. Furthermore, the government has instituted a comprehensive codified regulatory regime, whose primary function is to ensure investor confidence in the market by creating an open, fair and equitable securities market manipulation. The successful institution of these principles is essential to the prosperity of China's securities market.

If China seeks to experience continued economic growth into the 21st century, then it will have to open its market to the ideology of greater privatization and less government interfer-

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^{11.} See id.

^{12.} Id.

^{13.} See Wong, supra note 1, at 1221.

^{14.} See Cao, supra note 6, at 44.

^{15.} See id. at 13.

^{16.} See id. at 43.

^{17.} See Zhonghua Renmin Gongheguo Zhengquan Fa [Securities Law of the People's Republic of China] arts. 1-9, translated in Legislative Affairs Comm'n of the Standing Comm. of the Nat'l People's Congress of the People's Republic of China, The Laws of the People's Republic of China 1998, at 135-76 (1999) [hereinafter Securities Law]. See also Mo Zhang, China's New Securities Law: An Effort to Create Markets That Are Open and Equitable, E. Asian Exec. Rep., Feb. 15, 1999, at 9, 9.

^{18.} Securities Law, supra note 17, art. 3.

^{19.} Id. art. 5.

ence, and an economic structure in which the private sector, not the state, owns a majority interest in the nation's enterprises. The implementation of these economic reforms will produce greater incentives for its citizens to pursue operational efficiency, while corporate management will incur a sense of accountability to the private sector for the profits and losses of their business. Beijing must also allow its debt and equities markets to be driven by a policy of *laissez-faire*, in which market forces, not the state, determine the fate of the nation's enterprises and securities market, thereby producing a more efficient marketplace in China. If, however, the Party continues to pursue a policy of government interference, "then it will almost certainly guarantee the failure of the securities market in most respects, except of course, in the most short-term of objectives – capital infusion from the domestic and foreign shareholding public."20 Thus, to accomplish these ambitious goals, it will be necessary for China to improve upon its securities laws for the purpose of creating an environment that encourages these Western capitalist market theories.

However, with the implementation of these Western capitalist market theories into the Chinese marketplace, the survival of the Party will be at stake. The inherent conflict of one country having two systems – a communist government with a capitalist securities market structure – makes it impossible for the Party to retain control over China without disposing of its securities market. Since the Securities Law of the People's Republic of China ("Securities Law" or "Law") is subservient to Party ideology and objectives – primarily state control over the securities market and its participating enterprises – the Law does not work. Accordingly, either the securities market will fall or the current government will fall. Because its failing state-run economy is in dire need of capital, the government has no other alternative than to support the nation's securities market. Hence, it is inevitable that China's current government will fall at the expense of its capitalist securities market.

Part II of this Article discusses the transformation of the securities market's regulatory scheme in China from a decentralized regulatory system to a more centralized, national approach to securities regulation, resembling the U.S. model. This Part also briefly examines and analyzes the codification of China's first nationally instituted Securities Law, a subject that is discussed throughout the course of this Article. Part III examines China's Securities Law concerning its stock exchanges. In addition, this Part takes a close look at the Shanghai and Shenzhen Stock Exchanges and the problems associated with these exchanges.

Part IV scrutinizes China's employment of a "quota system" as well as the government's discretionary authority in approving applications to issue shares to the public. This Part also examines the burdensome state-imposed requirements that a company must first meet to even submit an application to issue shares. And finally, the author analyzes the price controls that the state places on newly issued securities in the primary and secondary markets. Part V examines the share structure and how all shares in China are not created equal. This Part further discusses the consequences of China's non-egalitarian, segregated share structure on the market.

Part VI illustrates China's changing policy toward the subject of hostile takeovers. This Part examines the early stages of the securities market, in which the government insulated management from the threat of a hostile takeover. It then discusses the Securities Law, which encourages these types of takeovers, as it prefers an ailing company to be taken over by a private company instead of going bankrupt and laying off its employees.

Part VII looks into China's insider trading legislation, and the problems experienced by the securities market due to the overlap between government and the private sector. The author also discusses the troubling notions posed by China's Securities Law on insider trading. Part VIII investigates China's disclosure laws and the government's attempt to bridge the information gap between the central government, listed companies and the investing community. This Part also examines the incentives of companies to disclose inaccurate and untrustworthy information, as it looks at the fraudulent activities of Chengdu Hongguang Industrial Company ("Chengdu"). In addition, it discusses the state's interference in the financial media and private sector, which has served to disrupt the effectiveness of company disclosures.

And finally, Part IX examines the failure of China's Securities Law to provide civil remedies for shareholders, an important mechanism for enforcing securities rules and regulations. This Part examines the benefits of private litigation, and the drawbacks of China's lack of a legal provision concerning civil remedies for shareholders.

II. THE REGULATORY REGIME

National security required that China's experimental endeavor into a market system be successful, since the capital expected to be produced by the securities market was to be used to refinance the nation's ailing state-sector.²¹ To accomplish this goal, it was necessary for China to install a regulatory regime that would efficiently govern the securities market and ensure investor confidence in the market. Thus, the securities division of the People's Bank of China ("PBOC"), which functioned as China's central bank, was initially allocated jurisdiction over the regulation of China's securities market.²² As the primary securities regulator in China, the PBOC employed a decentralized and fragmented approach toward its regulatory duties, and in doing so, delegated the day-to-day regulatory responsibilities to its various local provincial branches throughout the country.²³ For instance, the Shanghai and Shenzhen branches of the PBOC were responsible for managing, overseeing, supervising and coordinating securities market activities in their respective municipalities.²⁴ This noncentralized approach to securities regulation resulted in every region of China having its own distinguished set of rules governing their securities market.²⁵ As a result, the Shanghai and Shenzhen Stock Exchanges, and the regional trading centers,

^{21.} Anthony Zaloom & Hongchuan Liu, *A Legal Framework for Securities: Chinese Securities Law Finally Takes a Step Forward*, China Bus. Rev., May 1, 1999, at 27. *See also* Chengxi Yao, Stock Market and Futures Market in the People's Republic of China 77 (1998).

^{22.} See Tien-Yo Chao, Hong Kong and China, in Issuing Securities: A Guide to Securities Around the World, Int'l Fin. L. Rev. Special Supplement 24, 29 (1993); Jay Zhe Zhang, Securities Markets and Securities Regulation in China, 22 N.C. J. Int'l L. & Com. Reg. 557, 561-62 (1997).

^{23.} See Chao, supra note 22, at 29.

^{24.} Id.

^{25.} See YAO, supra note 21, at 77.

fell under the regulatory scheme of their local provincial governments.²⁶

As China's economy continued to experience unprecedented economic growth during the early part of the 1990's, the Party viewed the possibility of a stock market crash as a serious threat to its rule. As a result, on December 17, 1992, the State Council established a centralized regulatory scheme, which employed a two-tiered approach to securities regulation – the State Council Securities Committee ("SCSC") and the China Securities Regulatory Commission ("CSRC").²⁷

The SCSC acted as the supervisory authority for the overall administration of the country's securities market.²⁸ Its primary functions were: (1) to organize the drafting of securities laws and regulations; (2) to adopt policies and regulations in connection with the securities market; (3) to submit proposals to the State Council for developing the securities market; (4) to guide, coordinate, supervise and monitor the activities of the securities market; and (5) to supervise the CSRC.²⁹

The second tier CSRC took on the role as the regulatory branch of the SCSC, and was composed of experts from the securities industry.³⁰ Its primary functions were: (1) to draft regulations in connection with the administration of the securities market and to supervise securities institutions; (2) to supervise securities offerings and trading, as well as companies which have issued shares to the public; (3) to supervise the offering of securities outside of China by Chinese enterprises; (4) to work with other government authorities on securities statistics and securities market analysis; and (5) to report all findings and report all policy and rule proposals to the SCSC.³¹

As a result of this newly established regulatory regime, the role of the PBOC was mitigated to the mere approval and administration of securities institutions, which was circumscribed by the supervisory authority of the CSRC.³² Thereafter, in

^{26.} Chao, *supra* note 22, at 25.

^{27.} Tingting Tao, The Burgeoning Securities Investment Fund Industry in China: Its Development and Regulation, 13 Colum. J. Asian L. 203, 215 (1999).

^{28.} See Chao, supra note 22, at 30.

^{29.} See id.

^{30.} *Id*.

^{31.} *Id*.

^{32.} Id.

April 1993, China promulgated the Administration of the Issuing and Trading of Shares Tentative Regulations ("ISRs"), which was to govern the trading of securities on the Chinese stock exchanges.³³

Then, on April 28, 1994, China's CSRC took a step in the development of its securities market by signing a Memorandum of Understanding with the U.S. Securities and Exchange Commission ("SEC"), which was designed to "formalize a cooperative and consulting relationship" between both nations' securities regulatory authorities, with regard to the provision of technical and enforcement assistance.³⁴ As a result of this Memorandum of Understanding, China adopted many of the features of the U.S. model for securities regulation. For instance, China replaced its two-tier structure, which consisted of the SCSC and CSRC, with a single, unified system, in which the CSRC was directly subordinate to the State Council.³⁵ This is similar to the U.S. regulatory scheme, in which the SEC is directly subordinate to the executive branch. Moreover, China has adopted many American securities laws in its promulgation of the country's first comprehensive national Securities Law on December 29, 1998, which subsequently went into effect on July 1, 1999.36

This Securities Law, presently in effect in China, empowers the CSRC with the authority to implement a centralized and unified regulation of the nationwide securities market in order to ensure their lawful operation.³⁷ In doing so, this branch of government performs the following functions in the course of its regulation of the country's securities market: (1) formulates

^{33.} Gupiao Faxing Yu Jiaoyi Guanli Zanxing Tiaoli (Administration of the Issuing and Trading of Shares Tentative Regulations) arts. 1-2, translated in 7 China Law and Practice 23-44 (1993) [hereinafter ISRs]. See also Benjamin Chun, A Brief Comparison of the Chinese and United States Securities Regulations Governing Corporate Takeovers, 12 Colum. J. Asian L. 99 (1998).

^{34.} Press Release, U.S. Securities and Exchange Commission, SEC and China Securities Regulatory Commission Sign Memorandum of Understanding to Formalize Cooperative Relationship (Apr. 28, 1994), *available at* 1994 WL 150804.

^{35.} Daniel M. Anderson, *Taking Stock in China: Company Disclosure and Information in China's Stock Markets*, 88 GEO. L.J. 1919, 1928 (2000).

^{36.} See Xian Chu Zhang, The Old Problems, the New Law, and the Developing Market – A Preliminary Examination of the First Securities Law of the People's Republic of China, 33 Int'l L. 983 (1999).

^{37.} Securities Law, supra note 17, arts. 7, 166.

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rules and regulations concerning the regulation of the market; (2) carries out the examination, verification and approval process of applicants that endeavor to issue shares to the public; (3) regulates the offering, trading, registration, custody and clearing of securities; (4) regulates the securities business activities of all participants in the securities industry; (5) formulates the qualification standards and code of conduct for persons engaged in the securities business and supervises the same; (6) supervises and inspects the disclosure of information in connection with securities offering and trading; (7) directs and supervises the activities of the Securities Industry Association; 38 and (8) investigates and deals with violations of laws and administrative regulations concerning the regulation of the securities market. 39

The Securities Law empowers the CSRC with carte blanche authority in terms of its ability to investigate possible securities law violations, thereby enabling it to efficiently regulate the securities market and its participants. Hence, the CSRC has the ability to enter, at will, the site at which an illegal act has been committed to investigate and obtain evidence; interview persons in connection with the event under investigation; inspect and take copies of relevant documents and examine securities account information.⁴⁰ In addition, the person or persons under investigation are required to cooperate fully and truthfully with the CSRC, since the Law expressly prohibits them from obstructing the investigatory process.⁴¹ To ensure the impartiality, honesty and faithfulness of the CSRC, the working personnel of this regulatory authority are prohibited from simultaneously holding a position in the organization being regulated, as well as holding, purchasing or selling securities in the market during tenure.⁴² The staff is also prohibited from exploiting their position to obtain improper gains from participants in the securities industry.⁴³

The Securities Law is vital to the success of China's securities market, as it endeavors to "protect the lawful rights and

^{38.} See id. art. 164.

^{39.} Id. art. 167(1)-(7).

^{40.} Id. art. 168(3).

^{41.} Id. art. 171.

^{42.} Id. arts. 37, 174.

^{43.} Securities Law, supra note 17, art. 170.

interests of investors, safeguard the economic order and public interests of society and promote the development of the socialist market economy."⁴⁴ In addition, it serves to enhance the objectivity and transparency in China's securities regulatory process as well as to implement such themes as "fairness and equitability" into the market, so as to build consumer confidence.⁴⁵ However, the Law is destined to futility because of the inherent conflict between the Marxist socialist theories of the ruling Party and the Western capitalist theories of the nation's securities market. As a result, China's Securities Law is not worth the paper it is written on.

III. THE SHANGHAI AND SHENZHEN STOCK EXCHANGES

When the Shanghai and Shenzhen Stock Exchanges were first established in December 1990 and July 1991, respectively, they were regulated by their respective municipal governments as well as the local provincial branches of the PBOC. However, this regulatory scheme changed in July 1999, when the regulation of the two stock exchanges came under the jurisdiction of China's newly enacted Securities Law.⁴⁶ Under the Securities Law, a "stock exchange" is defined as a "non-profit legal person that provides a place for the centralized trading of securities at competing prices."⁴⁷ The Law also states that only securities companies that are members of a stock exchange are permitted to participate in the trading activity of securities at that stock exchange.⁴⁸

Analogous to the New York Stock Exchange, Inc., ("NYSE"), the objective of China's stock exchanges is to ensure the maintenance of a fair and orderly marketplace.⁴⁹ To achieve this goal, customer orders received on the floor of a Chinese stock exchange are required to be executed based on price instructions and time precedence, thereby outlawing any type of ineq-

^{44.} *Id.* art. 1.

^{45.} Id. art. 3.

^{46.} See China Sec. Regulatory Comm'n, 12 Order of the President of the People's Republic of China (1998), available at http://www.csrc.gov.cn/csrcsite/eng/elaws.htm (last visited Feb. 23, 2002).

^{47.} SECURITIES LAW, supra note 17, art. 95.

^{48.} *Id.* art. 103.

^{49.} N.Y. STOCK EXCH. R. 104, 2 N.Y. Stock Exch. Guide (CCH) \P 2104.10 (requiring specialists to maintain a "fair and orderly" market).

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uity or unfairness in the market.⁵⁰ The stock exchanges are also responsible for the timely dissemination of quotations concerning securities trading, which is for the purpose of enabling market participants to have equal access to trading information.⁵¹ To control speculative investing on the floor of the stock exchanges, market participants are prohibited from day trading, which encompasses the same day purchase and sale of a security, as well as any type of trading on margin.⁵² Furthermore, the stock exchanges have the authority to temporarily suspend trading in a particular security if a sudden event occurs which affects the normal conduct of securities trading.⁵³

Moreover, the stock exchanges are obligated to monitor the securities trading conducted on the floor of the exchange on a real-time basis, of which they are required to report any unusual trading activities to the CSRC.⁵⁴ Therefore, if a stock exchange recognizes a violation of the Securities Law or exchange rules by any one of its members, it has the authority to impose disciplinary proceedings against that member, which may include a permanent bar from trading on that exchange.⁵⁵ To further promote the objectives of the Securities Law, a stock exchange possesses the ability to formulate rules.⁵⁶

Similar to the trading structure of the NYSE, the Shanghai and Shenzhen Stock Exchanges operate in an auction market environment, although they do not employ a specialist or market-maker system.⁵⁷ Instead, the Shanghai Stock Exchange has a rule requiring its members, at its request, to engage in proprietary trading for the purpose of maintaining the continuity and stability of the trading market.⁵⁸ As such, the market risks associated with securities trading are born by all members.⁵⁹ The Shenzhen Stock Exchange, on the other hand, only requires that its members disclose their trading intentions before they engage in proprietary trading in excess of 300,000

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^{50.} See Securities Law, supra note 17, art. 105.

^{51.} See id. art. 107.

^{52.} See id. arts. 36, 106.

^{53.} See id. art. 109.

^{54.} Id. art. 110.

^{55.} *Id.* art. 116.

^{56.} SECURITIES LAW, supra note 17, art. 113.

^{57.} See YAO, supra note 21, at 40-41.

^{58.} *Id.* at 41.

^{59.} See id. at 40.

shares of the same type of share, or one million shares of the same security, within a period of three successive days.⁶⁰ However, aside from these requests by the Shanghai and Shenzhen Exchanges for the participation of their members in the trading market⁶¹ or the disclosure of their members' trading intentions,⁶² members are under no obligation to make a market in a security.⁶³

Although the Shanghai and Shenzhen Stock Exchanges appear to be very similar to the stock exchanges in the U.S., in that they provide for self-regulation of the securities market under the guidance of the government, they possess inherently distinguishable features. For instance, the fact that China's stock exchanges do not employ the Western concepts of a specialist or market-maker system is troubling. The proponents of specialist and market-maker systems claim they act to "sustain stability and increase liquidity" in the market, while critics contend that they hurt investors by allowing price manipulation and hurt issuers due to the increased costs that they exact from them.⁶⁴ However, the arguments against specialist and market-maker systems have so far proven fruitless in the U.S. due to the institution of rules and regulations that maintain affirmative obligations and restrictions on specialists and market-makers.⁶⁵ It is also troubling that the Securities Law makes no mention of the Western concept of "best execution."66 In addition, the notion that there is no rule prohibiting 'front running" (the trading ahead of customer orders, which possess priority, parity or precedence) is also troubling because it creates an inequity in the marketplace, which is in violation of the

^{60.} *Id.* at 41.

^{61.} *Id*.

^{62.} *Id*.

^{63.} See YAO, supra note 21, at 40.

^{64.} Id. at 56.

^{65.} See N.Y. STOCK EXCH. R. 104, 2 N.Y. Stock Exch. Guide (CCH) ¶ 2104.10.

^{66.} *Id.* (The function of a member acting as a regular specialist on the floor of the NYSE includes "the effective execution of commission orders entrusted to him."). *See also* Leslie Eaton, *Stock Trades: A Better Deal for Investors Isn't Simple*, N.Y. TIMES, Apr. 25, 1997, at D1. (The term "means that brokers must try to do their best to make sure that when customers buy a stock they pay the lowest price available and when they sell a stock they get the highest price.").

Securities Law.⁶⁷ Furthermore, China's stock exchanges have a rule which restricts members of one exchange from becoming members on another exchange.⁶⁸ This rule, coalesced with the rule which first requires a securities firm to become a member of an exchange prior to trading securities on that exchange functions to restrict a member of one exchange from trading on the floor of another. This is troubling because such a restriction on membership hurts the liquidity and competitive nature of the market. Hence, the Securities Law concerning stock exchanges is ineffective as it has proven itself to be inadequate in dealing with the self-regulatory aspect of its stock exchanges. This is due to the inherent conflict between the Marxist socialist theories of the ruling Party and the Western capitalist theories of a securities market, as the former has refused to implement certain Western market fundamentals into the framework of its Securities Law.

IV. PUBLIC ISSUANCE AND LISTING OF SECURITIES – THE QUOTA SYSTEM

With the goals of preserving state ownership over the marketplace and ensuring that shareholding companies act within the parameters of the socialist economic plan, the Party instituted a quota system governing the public issuance and listing of securities.⁶⁹ This system directs the State Council to determine, on an annual basis, the number of enterprises allowed to issue shares to the public. The State Council also determines the total amount of capital to be raised, as well as the size and

^{67.} Securities Law, *supra* note 17, art. 3 ("Securities shall be issued and traded in line with the principles of openness, fairness and equitability."). See also N.Y. Stock Exch. R. 90, 2 N.Y. Stock Exch. Guide (CCH) ¶ 2090 (stating that proprietary orders must be announced as such and yield priority, parity and precedence to any order which is for the account of a person who is not a member); N.Y. STOCK EXCH. R. 92, 2 N.Y. Stock Exch. Guide (CCH) ¶ 2092 (stating that no member shall personally trade or initiate the trade of any security on the NYSE for his own account while such member personally holds or has knowledge that his member organization holds an unexecuted customer order).

^{68.} See Provisional Rules Governing Members of Shanghai Securities Exchange, arts. 16-17 (1991), translated in Hainan Sec. Trading Ctr., A Collection of China Securities Statutes and Related Legal Documentation (1993).

^{69.} See Anderson, supra note 35, at 1942.

pricing of each offering.⁷⁰ Through the employment of this system, the Party has been able to successfully pursue a system of "limited privatization" in the makeup of its shareholding companies, by which the government has retained a majority state ownership (51% or greater interest) while permitting only minority private equity participation.⁷¹

To illustrate the process, a company seeking to issue securities to be listed on an exchange must first be selected by a provincial or ministerial office.⁷² This local government office is required to select companies in accordance with the annual quotas that have been pre-established by the central government.⁷³ Once a company has been selected, it must then submit an application as well as any other required documentation to the CSRC for its approval.⁷⁴ The CSRC is then responsible for establishing an "issuance examination commission,"⁷⁵ which must undertake an examination of the application materials, and then vote on the company's application.⁷⁶

The CSRC has significant discretionary authority in its final decision concerning the approval or disapproval of an application to issue shares to the public.⁷⁷ This discretion has exemplified China's bias toward the submission of applications by state-owned enterprises over that of the private sector.⁷⁸ Through these inequitable dealings, the government has been able to achieve its long standing position of reserving the functionality of the securities market for more state-concentrated objectives, i.e., the provision of capital for the cash-starved state sector.⁷⁹ The problem with this approval process is that it lacks a detailed, objective standard that is transparent to the public.⁸⁰ Thus, the Law's requirement that the government

^{70.} Yao, *supra* note 21, at 6-7.

^{71.} Ramsey, supra note 7, at 463.

^{72.} See Zaloom & Liu, supra note 21, at 28.

^{73.} Id.

^{74.} SECURITIES LAW, supra note 17, art. 11.

^{75.} *Id.* art. 14.

^{76.} Id. art. 15. See also Anderson, supra note 35, at 1941.

^{77.} Zaloom & Liu, supra note 21, at 28.

^{78.} See id.

^{79.} See id.

^{80.} See id.

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publish its reasons for denying an application becomes null and void.⁸¹ As Professor Lan Cao has noted:

The system thus appears arbitrary and capricious, as there [is] a sense that the state-controlled and state-supervised selection process further[s] less the economic interests of the investing public than the vested political interests of the well connected firms or those in sectors favored and promoted by the government. 82

As a result of this political favoritism, the CSRC has approved some low quality issues while high quality private enterprises have been denied their application to issue shares in China's securities market.

In an effort to resolve these problems, the Securities Law has introduced a more market-oriented response to the process of approving an application to issue shares to the public. For instance, Article 14 requires the CSRC to establish an "issuance examination commission," which is to be composed of its own professionals as well as industry experts.83 This committee is prohibited from having any material connection with the applicant, which includes anyone who has accepted a gift, such as shares, from the applicant.84 If the committee refuses to approve an applicant, then it must give reasons for its denial.85 However, if the committee approves an applicant, then it must make a disclosure of the company's documents for public inspection.⁸⁶ Following the approval of an application to issue shares to the public, the government relieves itself of any liability from changes in an issuer's operation or earnings by placing all responsibility for such changes on the issuer and all investment risks on the investor.87

China's newly enacted Securities Law has greatly improved the approval process for initial public offerings by: (1) adding greater transparency to the process, as the government is now required to disclose the applicant's documents for public in-

^{81.} See SECURITIES LAW, supra note 17, art. 16.

^{82.} Cao, *supra* note 6, at 48.

^{83.} SECURITIES LAW, supra note 17, art. 14.

^{84.} See id. art. 15.

^{85.} Id. art. 16.

^{86.} Id. art. 17.

^{87.} Id. art. 19.

spection upon approval⁸⁸ and publicize the reasons for its denial of an applicant;⁸⁹ (2) enhancing the qualities of listing companies, as industry experts will now be involved in the decision-making process;⁹⁰ and (3) putting the market participants on notice that there are risks in the market even though the government has approved a company's application to issue shares to the public, and that those risks are the responsibility of the issuer and investor.⁹¹

The process appears on its outskirts to be market-based, but, in practice, it is dependent on the whims of the government, which is empowered to exercise significant discretion over the process.⁹² Thus, the Law fails to remedy the inherent conflict between the current Chinese government and a capitalist securities market, in that the approval process maintains no standards of objectivity and no requirement that the decision to approve or disapprove of an application to issue shares to the public must be based on market theory and not state directives. Hence, there is ample opportunity for state officials to exercise their discretion by arbitrarily and capriciously approving the issuance of securities to further the government's political agenda, rather than appeasing the demands of the market. In other words, the government has an incentive to support its failing state-owned enterprises by approving their applications to issue shares to the public over that of private enterprises, even if the applicants do not meet the requisite credentials under the Law. To compound this problem, there is a lack of an appeals procedure in place for enterprises whose applications have been rejected.⁹³

However, before a company can even attempt to submit an application to issue securities to the public, it must first meet certain state-imposed requirements as detailed under the Company Law of the People's Republic of China ("Company Law") for the issue of new shares.⁹⁴ First, as a capital adequacy

^{88.} Id. art. 17.

^{89.} SECURITIES LAW, supra note 17, art. 16.

^{90.} Id. art. 14.

^{91.} Id. art. 19.

^{92.} Zaloom & Liu, supra note 21, at 28.

^{93.} See YAO, supra note 21, at 7.

^{94.} See Zhonghua Renmin Gongheguo Gongsi Fa [Company Law of the People's Republic of China] art. 152, translated in Legislative Affairs Comm'n of the Standing Comm. of the Nat'l People's Congress of the

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quacy requirement, a company must have a minimum of paidin registered capital totaling RMB 50 million yuan.⁹⁵ Second, the enterprise is required to have been continuously profitable for the previous three consecutive years. 96 Third, the enterprise may not have committed any serious illegal acts during the previous three consecutive years of operation.⁹⁷ Fourth and finally, the government maintains the discretion to approve the issuance of new shares.98 Although this type of regulation may be perceived as protecting the securities market from the admission of low quality, unsafe issues, it may also be construed as hindering some potentially lucrative companies from raising capital to pursue their business objectives. For example, the medical and pharmaceutical industries are sectors of the economy that have very large overhead, yet infinite potential for profits and for improving China's quality of life through the production of advanced medical and pharmaceutical products. Another strong example involves the Internet, which is an industry that has an infinite potential for profit and for improving the country's quality of life through the production of technological advancements in communications. The development of these industries are, however, adversely effected by their inability to raise capital through the issuance of stock in the Chinese securities market due to their failure to meet the country's minimum capital adequacy requirement and to demonstrate a minimum of three consecutive years of profitability.99 Hence, China should seriously consider reforming its Company Law in order to lower the barriers to issuing securities, and allow the market to determine whether a company, which

PEOPLE'S REPUBLIC OF CHINA, THE LAWS OF THE PEOPLE'S REPUBLIC OF CHINA 1993, at 269-318 (1995) [hereinafter COMPANY LAW]. China's Company Law was adopted by the 5th Session of the Standing Committee of the 8th National People's Congress, promulgated on December 29, 1993, and effective as of July 1, 1994, to standardize the organization and activities of Chinese companies. See also Securities Law, supra note 17, art. 20 ("To issue new shares, listed companies shall meet the conditions provided for in the Company Law for the issuance of new shares."); Mo Zhang, supra note 17, at 11.

^{95.} Company Law, *supra* note 94, art. 152(2).

^{96.} *Id.* art. 152(3).

^{97.} Id. art. 152(5).

^{98.} Id. art. 152(6).

^{99.} See id. art. 152(3).

seeks to raise capital to further its business objectives, should be allowed to issue shares to the public.

Once a company has been approved by the CSRC to issue shares to the public, the issuer must then seek the approval of a stock exchange.¹⁰⁰ Subsequent to such an approval, the issuer will hire an underwriter, which will be responsible for the distribution of its shares to the public.¹⁰¹ Article 131 of the Company Law requires that the distribution take place at par or above par, but never below par.¹⁰² However, to ensure the success of an initial public offering, the government artificially sets the company's price at a price-earnings ratio that is well below the company's actual price-earnings in the secondary market. 103 This has made investments in the primary market a risk-free event, 104 while creating a highly volatile and speculative trading environment in the secondary market. Thus, to constrain speculative investing in the secondary market, the government has imposed price ceilings and floors to limit the movement of a stock's price in a single day of trading.¹⁰⁵ For instance, government regulations stipulate that a stock's price may only fluctuate by 10% over or under the previous day's closing price in a single day. 106 Furthermore, the Shanghai and Shenzhen Stock Exchanges have imposed stricter price controls, restricting the movement of companies with poor financial records to 5% over or under the previous day's closing price.¹⁰⁷ As a result of these price controls, the market on the Shanghai Stock Exchange "only rose and never fell" prior to the middle of 1992.¹⁰⁸ These price controls have had an adverse affect on the market, distorting the pricing of securities, decreasing liquidity and creating an investor community that is unaware of the risks associated with trading securities.

Since China's Securities Law fails to establish market determinate standards for the approval and issuance of securities

^{100.} See Securities Law, supra note 17, art. 46.

^{101.} Id. art. 21.

^{102.} Company Law, supra note 94, art. 131.

^{103.} See Zaloom & Liu, supra note 21, at 28.

^{104.} *Id*.

^{105.} See Anderson, supra note 35, at 1943.

^{106.} Id. at 1944.

^{107.} Id.

^{108.} Ellen Hertz, The Trading Crowd: An Ethnography of the Shanghai Stock Market 35 (1998).

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as well as the secondary trading of new issues, the ruling Party has retained the luxury of being able to exploit its unilateral authority over the securities market in order to support its state-owned enterprises at the expense of the private sector. Thus, the Law is undermined by the discretionary authority of the government with respect to the approval and issuance of securities, and the government's manipulation of the secondary trading of new issues, as the Party insists on making China's market regulations subservient to the directives of the state.

V. CHINA'S SHARE STRUCTURE – ALL SHARES ARE NOT CREATED EQUAL

A Western capitalist market theory that "all shares are equal" has yet to be adopted by China's securities market. In the U.S., private enterprises are allowed to issue two kinds of stocks: common and preferred. The distinction between these two classes of stock can be characterized by one's dividend expectations, voting rights and priority in liquidation. Other than these three major differences, shareholders of each class of stock are entitled to equal rights and equal benefits. Similarly, in China, stocks are divided into various sets of classes. However, class distinctions between stocks are solely for the ideological purpose of maintaining the leading role of government in the economy, by compelling state and public organizations to hold the majority of shares.¹⁰⁹ Although the Securities Law provides the principal that the classification of similar shares must carry equal rights and equal benefits, 110 a de facto inequity has long existed between shareholders in China's æcurities market, which is based on investor identity and not economic factors.¹¹¹

To maintain the government's dominant position in the securities market, China has subdivided its share structure into four segregated groups: (1) state shares; (2) legal person shares ("C Shares"); (3) individual shares ("A Shares"); and (4) foreign

^{109.} Minkang Gu & Robert C. Art, Securitization of State Ownership: Chinese Securities Law, 18 Mich. J. Int'l L. 115, 127-28 (1996).

^{110.} Company Law, supra note 94, art. 130. See also Xian Chu Zhang, supra note 36, at 987.

^{111.} See Xian Chu Zhang, supra note 36, at 987.

investor shares ("B Shares").112 State shares refer to those shares obtained by either the state or an institution on behalf of the state, while legal person shares refer to those shares obtained by legal persons, which consists of entities created or recognized by law, as opposed to natural persons. 113 The public issuance of A Shares is reserved only for individual domestic Chinese investors, while B Shares are reserved exclusively for foreign investors, which includes Chinese citizens overseas.¹¹⁴ State shares and legal person shares, which account for approximately 60-70% of the total shares issued, are prohibited from being converted, transferred or traded in the securities market. 115 A Shares, on the other hand, can be traded on the securities market, although they only account for a small fraction of the total issued shares in China. Since the government is wary of allowing foreign companies access to its domestic securities market, for fear of losing control of its economy, foreign investors are limited to investing in the B Share market, as cross-trading between the A Share and B Share market is prohibited.¹¹⁶

This segregated market structure has enabled the government to maintain its leading role in the market, as it has kept foreigners and private citizens from acquiring control of China's listed companies. In other words, the inequity in shares has enabled the government to hold a majority of shares in all listed companies, while permitting only minority private equity participation in the market by Chinese citizens and foreigners. It has also insulated the stock market from the sudden outflow of capital that has set off crises in other developing

^{112.} Gufenzhi Qiye Shidian Banfa (Trial Measures on Share-formulated Enterprises) art. 4, translated in 2 China L. Foreign Bus. Reg. (CCH) ¶¶ 13-570–13-570(9) (May 2, 1993).

^{113.} Id. See also Gu & Art, supra note 109, at 128.

^{114.} See Guowuyuan Guanyu Gufen Youxian Gongsi Jingnei Shangshi Waizi Gu De Guiding (Regulations of the State Council on Foreign Capital Shares Listed in China by Companies Limited by Shares) arts. 3-4, translated in 2 China L. Foreign Bus. Reg. (CCH) ¶¶ 13-600–13-600(28) (Sept. 19, 1996). See also Mo Zhang, supra note 17, at 10.

^{115.} Tao, *supra* note 27, at 229.

^{116.} *Id*.

^{117.} See Craig S. Smith, China to Let Banks Set Own Interest Rates Over Next 3 Years, N.Y. Times, July 20, 2000, at C3.

countries.¹¹⁸ The consequence of such a market structure has been that widely dispersed individual investors with minority shareholdings are unable to monitor management's activities, and therefore, management has no incentive to increase the operational efficiency of their business.¹¹⁹ In addition, the Securities Law is silent on the issue of voting rights and protection for the minority shareholders in a listed company, which has placed the individual investor in a disproportionately inferior relationship with the majority shareholder – the state. Hence, most individual investors are far more likely to sell their shares if they are not satisfied with a company's performance, as they lack an alternative strategy for sharing their dissatisfaction with the company's management.¹²⁰

This compartmentalized share structure has also produced a separate set of forces of supply and demand, thus producing different prices and earnings ratios, and hence, different pricing for the same issue. For example, between 1992 and 1993, the index for A Shares received positive returns while the index for B Shares received negative returns, which adversely affected the trading volume and pricing of each share. Thus, B Shares tend to trade at a deep discount to the A Shares of the same company. This fragmented share structure has led to a flawed determination of investment value of issues in the secondary market, which has resulted in illegal arbitrage activities. Moreover, it has had the effect of creating a securities market with poor liquidity and price volatility, which has led to heightened speculation among the investor community.

Recently, China has been making some noise about merging the A Share and B Share market, which has led to a strong performance in the B Share market.¹²⁴ In 2000, when markets worldwide were incurring steep losses, two of the best performers were China's Shanghai and Shenzhen Markets.¹²⁵ Thus, a

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^{118.} *Id*.

^{119.} See Tao, supra note 27, at 231.

^{120.} *Id*.

^{121.} See YAO, supra note 21, at 22.

^{122.} Ramsey, supra note 7, at 477.

^{123.} See Craig Karmin, China's Shenzhen, Shanghai B-Share Markets Surged in 2000, May Be Merged for A Shares, Wall St. J., Nov. 6, 2000, at C16.

^{124.} Id.

^{125.} Id.

unification of China's A Shares and B Shares would surely increase the liquidity of China's securities market, as foreigners would then have access to the A Shares, while simultaneously working to eliminate the price disparity between markets for the same issue.

Even though the Securities Law theoretically embraces the Western capitalist market theory of equality amongst shares, 126 the securities market, under the guidance of the ruling Party, does not. Instead, the Party has maintained a segregated share structure between individual Chinese investors and foreign investors in order to maintain its majority ownership in listed companies so as to preserve government control over China's infrastructure and economy. Hence, the segregation of China's share structure has undermined the Securities Law in that it has allowed the government to retain control over the securities market to the point that it is guided by state directives at the expense of the market forces of supply and demand.

VI. HOSTILE TAKEOVERS

To further China's goal of majority state ownership and minority private equity participation in the stock market, the ISRs, promulgated in 1993 (predominantly superceded by the Securities Law in 1999), prohibited an "individual" investor from holding more than 0.5% of the total number of shares outstanding of the common stock of a listed company. A violation of the ISRs gave the issuer the legal right to purchase the excess portion of shares, with the approval of the CSRC, at a price that was the lower of the market price or the individual's original purchase price. The ISRs not only worked to stifle individual investment in the securities market, but also diminished the liquidity of the market while increasing price volatility. This led to heightened speculation among the investor community.

The ISRs provided that a shareholder, who had acquired 5% of a listed company, was required to disclose his security holding position within three business days of acquiring the posi-

^{126.} See SECURITIES LAW, supra note 17, ch. I.

^{127.} ISRs, *supra* note 33, art. 46. *See also* Shen Sibao, Legal Aspects of Doing Business in China 284 (1999); Chun, *supra* note 33, at 105.

^{128.} ISRs, *supra* note 33, art. 46.

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tion.¹²⁹ Thereafter, that 5% shareholder was required to disclose his position within three business days after every 2% change in ownership.¹³⁰ Furthermore, the ISRs specified that the shareholder was prohibited from trading more shares during the period prior to the date that he was required to disclose his position, and for two working days thereafter, so that the market would have an opportunity to gain awareness of his ownership position.¹³¹

Once the shareholder had acquired 30% of the issued shares of a listed company, he was obligated to make a tender offer, in cash, to all of the shareholders at a mandatory tender offer price.¹³² This mandatory tender offer price was the greater of either the highest price paid by the acquirer for its shares during the twelve months preceding the tender offer, or the average market price of such shares during the preceding thirty working day period.¹³³ Once the tender offer had been initiated, the acquirer was restricted from purchasing more shares of the targeted company.¹³⁴ To ensure full participation by the targeted shareholders during the period of tender offer, the acquirer was required to disclose all material information concerning itself and the tender offer.¹³⁵ A shareholder, who had tendered his shares, still retained the right to withdraw his shares from the tender offer, and instead, participate on a pro rata basis. 136 In other words, under the pro rata rule, a shareholder retained the right to change his mind with respect to a tender offer, and yet, the bidder was still required to buy in the same proportion from each shareholder, irrespective of a first come, first serve basis. 137

At the expiration of the tender offer, if the acquirer had less than a majority ownership of the targeted company, he was then permitted to purchase only an additional 5% of the targeted company's outstanding shares each year.¹³⁸ If, however,

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^{129.} Id. art. 47.

^{130.} *Id*.

^{131.} *Id*.¶ 2.

^{132.} Id. art. 48.

^{133.} *Id*.

^{134.} ISRs, *supra* note 33, art. 48.

^{135.} Id. art. 49.

^{136.} Id. arts. 51-52.

^{137.} Id.

 $^{138. \ \}textit{Id.} \ \text{art.} \ 51.$

the acquirer retained a majority ownership of the targeted company's outstanding shares, the shareholders, who had yet to tender their shares, maintained the right to have the tender offer extended. This extension of the tender offer was to prohibit a freeze-out merger in which the remaining shareholders would have been forced to sell their shares on less favorable terms than those of the tender offer. 140

Although the ISRs afforded targeted shareholders greater protection from hostile takeovers, they also worked to "insulate management from the external threats to their continued employment" by discouraging such takeovers.141 This was evidenced by Shenzhen Bao An Enterprises' failed takeover attempt of Shanghai Yanzhong Industrial, and Shenzhen Vanke's failed takeover attempt of Shanghai Shenhua Industrial in 1993, when the regulations were enacted. This antitakeover environment created an inefficient marketplace in China, as managers were not held accountable for their company's performance, and therefore, they had no incentive to maintain a more profitable enterprise. Thus, the shareholders had neither a method of monitoring the performance of managers, nor a method of demonstrating their disagreement with management by taking steps to retain control of the company through the takeover process.

With the promulgation of the Securities Law, the CSRC has signaled a change in China's attitude toward the takeover process, as it would rather see its failing state-owned enterprises be acquired by another company than go bankrupt and have its employees laid off. As an example of this policy change, the new Law eliminated the prohibition of a natural person owning more than 0.5% of a company's total outstanding shares, thereby favoring the right of the investor community to use its excess capital to acquire shares of listed companies. In addition, Article 79 of the new Law stipulates that after an investor has publicly announced his acquisition of 5% of a targeted company, he is then required to announce

^{139.} Id.

^{140.} ISRs, *supra* note 33, art. 51.

^{141.} Chun, *supra* note 33, at 117-18.

^{142.} See id. at 99-102.

^{143.} See Zaloom & Liu, supra note 21, at 28.

^{144.} Id.

every time his shareholdings therein have changed by 5%, and not 2% as previously required under the ISRs. However, the acquiring shareholder is still restricted from purchasing or selling shares of the targeted company during the period that he is required to disclose his ownership position. He

Moreover, when the investor has acquired 30% of a company, Article 81 of the Securities Law permits him to make a request to the State Council's securities regulatory authority for an exemption from the requirement that he offer to purchase all outstanding stock of the company. If, however, the investor is determined to be non-exempt from such an obligation, then the Law requires the 30% shareholder to make a tender offer, either through the use of stock or cash. Additionally, it eliminates the restrictions on the pricing of a tender offer, although prior approval from the CSRC is still required. Finally, the Law recognizes, in Articles 78 and 89, acquisitions by alternative methods, such as negotiations and private agreements.

This new, more relaxed Securities Law has avidly advocated a takeover-friendly environment in China. By encouraging hostile takeovers, the Law has put forward into the market-place the popular Western capitalist theme of "survival of the fittest." Instead of China continuing to pursue the expensive policy of protecting its state-owned enterprises from the prospects of a takeover, its economy is now to be determined more by market-oriented factors, in which management is to be held accountable for the performance of their business. China could still, however, go a step further in promoting the takeover process by amending Article 87 and allowing an acquirer to conduct a freeze-out merger following his acquisition of 90% of the target's stock. The government could also amend Article 79 in a manner analogous to the Williams Act. By doing so, the government would increase the period that the acquirer has to

^{145.} SECURITIES LAW, supra note 17, art. 79.

^{146.} *Id*.

^{147.} Id. art. 81. See also Zaloom & Liu, supra note 21, at 28.

^{148.} SECURITIES LAW, supra note 17, art. 81.

^{149.} See Zaloom & Liu, supra note 21, at 28.

^{150.} Id.

^{151.} See Securities Law, supra note 17, arts. 78, 89.

^{152.} See 15 U.S.C. § 78m(d) (2000) (this section is also known as 13(d)).

disclose his position from three to ten days, and permit the acquirer to purchase the targeted company's shares during that disclosure period, even though the price would not accurately reflect the company's information.¹⁵³ These amendments would, in turn, introduce a profit incentive to the takeover process, thereby producing a more economically efficient marketplace governed by the common prophecy of "manage your business profitably or suffer the consequences of being taken over by your investors or competitors."

Since China reasserted sovereignty over the former British colony, Hong Kong, on July 1, 1997, Chinese enterprises have migrated to Hong Kong to list H shares ("H Shares") on its stock exchange, beyond the reach of Beijing's regulators, who tend to regulate takeovers far more extensively than Hong Kong.¹⁵⁴ In spite of this mass migration of Chinese companies, Beijing has pledged to leave intact Hong Kong's highly Western capitalist market structure, which is loosely regulated in connection with market theory, in comparison to Beijing's stringent state regulation of its market.¹⁵⁵ Beijing has, however, asserted its control over the Hong Kong takeover process by making its consent to all takeovers and mergers a necessity, in order to soften the government's "fears that state assets were leaking away to foreign investors."¹⁵⁶

Although the Securities Law has taken giant steps in improving its mergers and acquisition process through deregulation, it still has not gone far enough in the direction of a securities market that is primarily based on market theory and not state directives. As a result, the shortcomings of China's Secu-

^{153.} See Chun, supra note 33, at 102.

^{154.} See Mo Zhang, supra note 17, at 10 (stating that H Shares are shares denominated in foreign currencies and registered in China, but issued and traded in Hong Kong).

^{155.} Berry Fong-Chung Hsu, Legislative Control of Hong Kong Financial Markets: Some Aspects of Banking and Securities Regulations, 28 IAW & POLY INT'L BUS. 649, 651-53 (1997). Under the guidance of the British-Chinese Joint Declaration, China's National People's Congress enacted Hong Kong's Basic Law on April 4, 1990, thus guaranteeing the existence of a one nation, two system paradigm between Hong Kong and China. Id. at 651-52. This acted to preserve the rule of law in Hong Kong for fifty years after the passage of Hong Kong to Chinese sovereignty. Id.

^{156.} Nathan N. McMurtray, Enforcing Voluntary Compliance: The Need to Strengthen Hong Kong's Merger and Acquisition Regulations, 12 COLUM. J. ASIAN L. 75, 89-90 (1998).

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rities Law with respect to the mergers and acquisition process has resulted in the migration of Chinese red chip companies to Hong Kong.

VII. INSIDER TRADING

Article 5 of the Securities Law prohibits fraudulent trading practices, such as insider trading and manipulation of the æcurities trading market.¹⁵⁷ Insider trading is contrary to the basic principles of equity and fairness, which govern the securities market.¹⁵⁸ The problem in China is that there is a public-private overlap because the central government is the largest investor in the securities market. This overlap between the Chinese government and listed companies encourages insider trading as government officials are in a position to make large profits on the inside information of future political and economic events.¹⁵⁹ In addition, the cultural weight placed on personal relationships encourages insider trading between those persons having connections with government agencies or issuing joint-stock companies.

For instance, the trading bond futures fiasco in 1995 was one of the worst incidents of insider trading in Chinese history, as it subsequently led to the closing of the country's financial futures market. In this incident, the three-year 1992 treasury bonds underlying Contract No. 327 were issued with a coupon rate of 9.5%. In the Shanghai International Securities Company ("SISCO") had decided to pursue an investment strategy of building a very large short position in the treasury bonds underlying Contract No. 327. Subsequently, the Ministry of Finance took various economic initiatives, which had the affect of substantially raising the contract's coupon rate. This monetary policy undertaken by the government resulted in

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^{157.} SECURITIES LAW, supra note 17, art. 5.

^{158.} Id. art. 3. See also Brian Daly, Of Shares, Securities, and Stakes: The Chinese Insider Trading Law and the Stakeholder Theory of Legal Analysis, 11 Am. U. Int'l L. Rev. 971, 994 (1996).

^{159.} See Daly, supra note 158, at 1008.

^{160.} YAO, *supra* note 21, at 103.

^{161.} Id. at 103-04.

^{162.} Id. at 104.

^{163.} Id.

large losses for SISCO.¹⁶⁴ In the end, the Shanghai Municipal Enterprise, a provincial government entity that owned SISCO, claimed itself to be the biggest loser on the contract, while the Ministry of Finance, which owned China Economic Development Trust & Investment Company, was considered the biggest winner in the deal.¹⁶⁵ This led, however, to insider trading allegations against the Ministry of Finance.¹⁶⁶ Dr. Xie Ping, Deputy Director of the Policy Research Department of the PBOC, noted that "the public ownership system ha[d] provided a gambling house for those with their hands on the public funds."¹⁶⁷

In response to these kinds of fraudulent trading incidents in the securities market, China instituted into its Securities Law several comprehensive provisions dealing with fraudulent trading practices, such as insider trading. With respect to the legal provisions dealing with insider trading, Article 68 expressly defines the following persons as "insiders":

- (1) Directors, supervisors, managers, deputy managers and other senior management persons concerned of companies that has issued shares or corporate bonds;
- (2) shareholders who hold not less than [5%] of the shares in a company;
- (3) the senior management persons of the holding company of a company that issues shares;
- (4) persons who are able to obtain company information concerning the trading of its securities by virtue of the positions they hold in the company;
- (5) staff members of the securities regulatory authority, and other persons who administer securities trading pursuant to their statutory duties;
- (6) the relevant staff members of public intermediary organizations that participate in securities trading . . . and the relevant staff members of securities registration and clearing institutions and securities trading service organizations; and
- (7) other persons specified by the securities regulatory authority under the State Council. 168

^{164.} Id.

^{165.} Id.

^{166.} See YAO, supra note 21, at 104.

^{167.} *Id*.

^{168.} Securities Law, supra note 17, art. 68.

Article 69 goes one step further and expressly defines "inside information" as "information that . . . is not made public . . . and concerns the company's business or financial affairs or may have a major effect on the market price of the company's securities." It further provides that the following information is "inside information":

- (1) [T]he major events described in the second paragraph of Article 62 of this law;
- (2) company plans concerning distribution of dividends or increase of capital;
 - (3) major changes in the company's equity structure;
 - (4) major changes in security for the company's debts;
- (5) any single mortgage, sale or write-off of a major asset used in the business of the company that exceeds [30%] of the said asset;
- (6) potential liability for major losses to be assumed in accordance with law as a result of an act committed by a company's director(s), supervisor(s), manager, deputy manager(s) or other senior management person(s);
 - (7) plans concerning the takeover of listed companies; and
- (8) other important information determined by the securities regulatory authority under the State Council to have a marked effect on the trading prices of securities.¹⁷⁰

Article 70 then compounds the definition of an insider and inside information with the provision that insiders and other persons who have unlawfully obtained inside information are prohibited from trading securities of the company on which he has inside information, disclosing the information or suggesting others to trade the securities.¹⁷¹

Article 37 provides that: "Employees of stock exchanges, securities companies, and securities registration and clearing institutions, staff members of the securities regulatory authorities, and other persons prohibited by laws . . . from participating in share trading, may not, while in office or during the statutory period, hold, purchase or sell shares." ¹⁷²

^{169.} Id. art. 69.

^{170.} Id.

^{171.} See id. art. 70.

^{172.} Id. art. 37.

Moreover, in an effort to further protect the Chinese securities market from insider trading violations, Article 39 provides that:

Professional institutions and individuals that produce documents such as audit reports, asset appraisal reports and legal opinions for share issuance may not purchase or sell the shares in question during the underwriting period for such shares and for a period of six months after the expiration thereof.

In addition to the provisions of the preceding paragraph, professional institutions and individuals that produce documents such as audit reports, asset appraisal reports or legal opinions, for listed companies may not purchase or sell the shares in question from the date on which they accept the entrustment by the listed company to the sixth day after the said documents are made public. ¹⁷³

Finally, Article 65 provides that no one may divulge the contents of a company's disclosure before such disclosure has been made public.¹⁷⁴ In its enforcement of these laws governing insider trading violations, China has instituted provisions in its legal system that make an insider trading violator subject to both civil and criminal liability.¹⁷⁵

What is troubling about China's legal provisions concerning insider trading is its ambiguous approach toward government officials, who are of particular concern since their positions overlap with that of the private sector. For instance, although the definition of an insider extends to "employees of the securities regulatory authority," 176 it does not include other types of government officials. 177 However, this loophole is remedied by Article 70, which extends its coverage to tippees, thereby providing that an informed person who learns of important company information may be prohibited from trading on that inside information. 178 It is even more troubling that government information may not fit the definition of "inside information" as provided by Article 69, even though prior knowledge of gov-

^{173.} Id. art. 39.

^{174.} SECURITIES LAW, supra note 17, art. 65.

^{175.} See id. art. 183.

^{176.} Id. art. 37.

^{177.} Anderson, supra note 35, at 1948.

^{178.} See Securities Law, supra note 17, art. 70.

ernment policies can provide officials with a trading advantage.¹⁷⁹ Also problematic is the notion that many securities institutions and their staff are completely excluded from participating in the securities market. This exclusionary provision of the new Law not only causes harm to the liquidity of the securities market in the short-term, but it also hinders the development of the securities market in the long-term. It is pragmatically feasible, as demonstrated by American securities laws, to deter insider trading while simultaneously allowing securities institutions and their staff to actively participate in the securities market.

Aside from these troubling aspects of the Securities Law, China has shown tremendous resilience in its commitment to explicitly prohibit insider trading violations, which has been demonstrated by its in-depth legal provisions and civil and criminal enforcement of such fraudulent activities. However, despite the comprehensiveness of China's codification of its prohibition of insider trading practices, government corruption remains the largest factor plaguing the securities market in China. Insider trading is a side effect of the inherent conflict between the Marxist socialist theories of the ruling Party and the Western capitalist theories of a securities market. The underlying principal of communism – a nationalized and centrally planned economy – has allowed the government to stand on both the regulatory and retail sides of the market, which poses a conflict of interest that the Securities Law has so far been unable to remedy.

VIII. DISCLOSURE

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The ruling Party is renown for fearing transparency and craving secrecy. However, with the promulgation of its new Securities Law, China has made great progress in its efforts to promote transparency in the marketplace, thus breaking "the managers' monopoly over corporate information." To protect the interests of investors, thereby building much improved domestic and foreign investor confidence in the market, the Law has taken huge steps to decrease the information deficit be-

^{179.} Id. art. 69. See also Anderson, supra note 35, at 1948.

^{180.} Anderson, supra note 35, at 1935.

tween the central government, the issuing companies and the investing public.

In pursuit of this mission, the Securities Law requires Chinese companies to provide certain documents to regulating bodies when registering to issue shares to the public.¹⁸¹ When the company is finally approved to issue shares, it must then disclose a share prospectus for public inspection. 182 The Law also includes provisions for continuous disclosure of company information through the publication of a semiannual, annual and material events report (any material event that may effect the price of the stock).¹⁸³ Additionally, the Law has removed the provision that previously exempted a company from disclosure if, in its own judgment, the disclosure would have been detrimental to the company while having no effect on the market price.¹⁸⁴ In doing away with this exemption, listed companies no longer have any discretion in their determination of whether or not to report an event to the regulatory authorities and the public.

Moreover, all shareholders are now required to disclose their ownership position to the CSRC and the public if it is equivalent to 5% of the outstanding stock of a listed company, as well as every time their ownership position increases by an additional 5%. In addition, when a shareholder's ownership position in a listed company reaches the 30% level, that shareholder is required to make a tender offer and disclose any relevant information concerning himself and the tender offer to the CSRC and public, unless the acquiring shareholder's request for an exemption from such an obligation is granted by the State Council's securities regulatory authority. 186

The use of different and often less stringent accounting standards by Chinese firms that do not comply with international standards have negatively impacted foreign direct investment into China's securities market, as it has made it harder for in-

^{181.} Securities Law, supra note 17, art. 11. See also Anderson, supra note 35, at 1925.

^{182.} See Securities Law, supra note 17, arts. 17, 58.

^{183.} Id. arts. 60-62. See also Anderson, supra note 35, at 1927.

^{184.} Anderson, supra note 35, at 1929.

^{185.} Securities Law, supra note 17, art. 41. See also Anderson, supra note 35, at 1929.

^{186.} See Securities Law, supra note 17, arts. 81-82; Anderson, supra note 35, at 1930.

vestors to accurately value listed Chinese companies.¹⁸⁷ This is due to the fact that investors are fearful that the companies are in possession of hidden liabilities.¹⁸⁸ In addition, the incentives for a company and its management to disclose inaccurate information or to make an omission in its disclosures are great. 189 For instance, in 1997, Chengdu was found by the CSRC to have falsely reported its 1996 profits, underreported its 1997 deficit and concealed the problems associated with its production line prior to its offering. 190 The company was also found to have used the proceeds from their offering contrary to that which was specified in their prospectus, and illegally used the funds from the offering to trade its own securities in 217 individual securities accounts.¹⁹¹ These false disclosures were authorized by the insiders of Chengdu in order to gain approval from the government to issue shares to the public. 192 As a result, the company, its underwriter and accounting firm were fined, and Chengdu's directors and officers were either banned from holding a high level position in a publicly traded company or received cautionary war nings.¹⁹³

The Securities Law has taken various steps to halt the incentives of management to disclose inaccurate information or to omit from disclosing information. For instance, Article 59 provides that "the documents for the issuing and listing of shares... announced by companies shall be truthful, accurate and complete." Furthermore, Article 72 provides that working personnel of the government, news media and relevant persons (persons employed in the securities industry) are prohibited from fabricating and disseminating false or misleading information that seriously affects securities trading. As an enforcement measure, Article 63 provides that an issuer who reports false or misleading information or omits to report information, thereby creating a disturbance in the order of the secu-

^{187.} McMurtray, supra note 156, at 83.

^{188.} Id

^{189.} See Anderson, supra note 35, at 1931.

^{190.} Id. at 1933.

^{191.} Id.

^{192.} Id.

^{193.} Id.

^{194.} Securities Law, supra note 17, art. 59.

^{195.} Id. art. 72.

rities market, will be liable for damages. ¹⁹⁶ In addition, "the responsible director(s), supervisor(s) and/or manager of the issuer or the company shall be jointly and severally liable for such losses." ¹⁹⁷ Violators of the disclosure regulations may also be subjected to criminal liability, which can encompass a term of five to ten years in prison. ¹⁹⁸ Moreover, the Law may subject persons other than management (accountants, lawyers and intermediaries) to civil and criminal liability if they allow the fraud to occur. ¹⁹⁹ Thus, the Law requires that these third parties act as "gatekeepers," policing the quality of information disclosures in the marketplace. ²⁰⁰

The problem regarding inaccurate and untrustworthy company disclosures is an even greater problem in China when compared to Western capitalist countries, as it has always been a mission of the communist regime to exploit its relationship with the public and private sectors in order to influence and control the securities market. For instance, all company disclosures must be reported to the public through financial publications in the state-owned media. Consequentially, the government's control over the financial media has diminished the effectiveness of a company's mandatory disclosure. It has reduced investor confidence in company information and the market, since investors do not know whether the company information is accurate or a product of government exploitation.²⁰¹ Additionally, there is the problem of the government possessing an intimate relationship with the private sector. As a result, state interference in the media and private sector has limited the impact of company information on the market prices of securities, as investors instead look to the prevailing state policies when valuing company information.²⁰²

^{196.} Id. art. 63.

^{197.} *Id*.

^{198.} See Zhonghua Renmin Gongheguo Xianfa [Criminal Law of the People's Republic of China] art. 181, translated in Legislative Affairs Comm'n of the Standing Comm. of the Nat'l People's Congress of the People's Republic of China, The Laws of the People's Republic of China 1997, at 21-149 (1998).

^{199.} See Securities Law, supra note 17, art. 202.

^{200.} Anderson, supra note 35, at 1939.

^{201.} See id. at 1950.

^{202.} See id. at 1920.

The disclosure of inaccurate and untrustworthy company information is a side effect of the inherent conflict between the Marxist socialist theories of the ruling Party and the Western capitalist theories of a securities market. The underlying principal of communism — a nationalized and centrally planned economy — which endorses the government's ownership of the media and the private sector, poses a conflict of interest that the Securities Law has so far failed to remedy. As long as the government continues to influence market information by way of its state-owned media and involvement in the private sector, investors will be unable to rely on a company's disclosure when making their investment decisions.²⁰³ Thus, it is mandatory that China completely privatize its financial media and sever Beijing's controlling relationship over the private sector in order to establish investor confidence in company disclosures.

IX. PRIVATE LITIGATION

The Securities Law does not explicitly create a private cause of action for shareholders.²⁰⁴ Furthermore, "the Company Law does not provide for derivative actions, or the fiduciary duty and duty of care of corporate directors, let alone for oppression remedies" for shareholders.²⁰⁵ As a result, the legal system in China has failed to provide civil remedies for shareholders, such as derivative suits, which would allow shareholders to sue a company and its directors and officers.

"Effective private remedies have proved to be an indispensable and essential part of securities law enforcement." Private remedies not only help to compensate defrauded investors, but also provide a deterrence against securities fraud and other misconduct, thereby supplementing the enforcement activities of the regulatory bodies, which are under-staffed and undertrained, to clean up the abuses of the securities market. In addition, they provide "direct incentives not only for market participants to refrain from violating securities laws, but also

^{203.} See id. at 1937.

^{204.} See Cao, supra note 6, at 53.

^{205.} Wenhai Cai, Private Securities Litigation in China: Of Prominence and Problems, 13 Colum. J. Asian L. 135, 143-44 (1999).

^{206.} Id. at 136.

^{207.} Id.

for victimized investors to detect, report and assist in the apprehension and prosecution of violators."²⁰⁸

It is highly unlikely that the police or prosecutors, who normally take over an allegation of securities fraud from the CSRC once it has been determined to be a crime, will take securities fraud as seriously as they do murders and robberies, as they are already overburdened with a large caseload. Additionally, the CSRC is risk-averse to being overturned by judicial review, and therefore, it is more likely to sacrifice the severity of sanctions for the certainty of its penalties, and it will pursue only cases with a high probability of conviction. Without a private right of action, individual shareholders may be "without redress for egregious, even criminal, behavior on the part of management." Therefore, if China is serious about enforcing its Company Law and Securities Law, then it must explicitly render to its shareholders the ability to raise a private cause of action against a listed company and its officers and directors.

The lack of an express or implied private cause of action for shareholders is arguably a product of communism, which preaches the ideal that the ruling Party is a government of the People, and that the nation's land and institutions are wholly owned by its citizens. Therefore, there is no reason for a private cause of action, since, when the government sues a company for failure to comply with the Securities Law, it is filing suit against the company on behalf of the People. On the other hand, Western capitalist securities markets endorse a private cause of action in certain matters, such as insider trading violations. This demonstrates the inherent conflict between Marxist socialist theories and the Western capitalist theories of a securities market. Hence, China's Securities Law once again falls short, as its regulatory regime, the CSRC, is unable to enforce its provisions due to an untrained and minimally sized staff. And yet, it refuses to seek the supplementary assistance of shareholders in its enforcement efforts.

^{208.} Id. at 142.

^{209.} See id. at 140.

^{210.} See id. at 140-41.

^{211.} Anderson, supra note 35, at 1940.

X. CONCLUSION

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China finds itself, once again, engrossed in economic turmoil, due to its failing state-run economy and its need for increased capital inflow. One of China's greatest and most immediate problems concerns its bankrupt pension system, which has become one of the main causes of the growing urban unrest amongst its citizens.²¹² The primary problem with China's failing pension system is the government's "one-child policy, coupled with longer life expectancy, [which] means the number of retired workers will grow much faster than the number of newly employed paying into China's pension system."²¹³ In an effort to maintain its promises from the Revolution of 1949, in which the Party pledged "cradle-to-grave support" (guaranteed housing, education, employment, medical care and retirement income to all Chinese citizens), China has been forced to embrace some groundbreaking economic reforms.²¹⁴ These reforms have consisted of a more market-oriented approach concerning the Chinese securities market, with greater foreign assistance. 215 Aside from handing responsibility for pension payments to its private sector (banks and securities institutions), Beijing must also allow foreign professionals to enter the Chinese securities market to manage its pension money.²¹⁶ Already, foreign asset managers, such as State Street Corporation and J.P. Morgan Chase & Co., are in the process of assisting China in launching its first mutual funds, and it is expected that more American companies will soon assist China in setting up its citizens' retirement securities accounts.217 Thus, it is apparent that the best mechanism for change in China is the failure of its state-run economy, as such financial difficulties provide the impetus for unprecedented economic reform in the country's securities market.

China's recently asserted sovereignty over Hong Kong should also have a positive effect on China's transition to a free and open market economy. The Hong Kong Stock Exchange is re-

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^{212.} See Karby Leggett, China Pension System is Cause for Increasing Agitation, WALL St. J., Oct. 30, 2000, at A24.

^{213.} *Id*.

^{214.} See id.

^{215.} See id.

^{216.} See id.

^{217.} See id.

nown for being an international marketplace for securities trading, as it is second in Asia only to the Tokyo Stock Exchange.²¹⁸ Hong Kong also presently reflects the territory's special position as a gateway to the vast economic hinterland of China, in that it is a forum for channeling foreign investment into the mainland's red chip companies. Additionally, it has provided China with a channel to engage in securities trading with the international community, particularly the West. For instance, H.C. Lee, chairman of the Hong Kong Stock Exchange, and Frank G. Zarb, chairman of the Nasdaq Stock Market, Inc., recently agreed to co-list their securities on each other's markets.²¹⁹ Thus, such prized American companies as Intel Corporation, Microsoft Corporation, Cisco Systems Inc., Dell Computer Corporation and Applied Materials, Inc., will be permitted to trade on the Hong Kong Stock Exchange. This should have the effect not only of increasing the market's 1quidity and foreign investment in China, but also of putting the U.S. markets at the back door of mainland China, where they can further affect reform in China's securities market. Beijing's promise to preserve the culture of Hong Kong following the resumption of Chinese sovereignty²²⁰ sets the stage for a gradual integration of these two distinct markets. This should have a positive effect on Chinese securities regulation, as enhanced competition between China's Shanghai and Shenzhen Stock Exchanges and the Hong Kong Stock Exchange will result in a deregulation of the country's securities market. Hence, China's securities market will become regulated by market forces rather than state interference.

Moreover, China's membership in the World Trade Organization²²¹ will likely have the effect of further liberalizing its securities market, as it will place China under the scope and scrutiny of a Western international trade group, which requires its members to adopt a more capitalist market approach to economic issues. This Western style free market economy has, so

^{218.} See Nasdaq and Hong Kong Stock Markets Agree to Share Listings, N.Y. Times, Dec. 14, 1999, at C10.

^{219.} Id.

^{220.} See Hsu, supra note 155, at 651-53.

^{221.} See Press Release, World Trade Organization, WTO Ministerial Conference Approves China's Accession (Nov. 10, 2001), available at http://www.wto.org/english/news_e/pres01_e/pr252_e.htm.

far, been received with open arms by the citizens of China, as they enjoy the benefit of being able to invest their savings in their country's red chip companies, as well as the world's blue chip companies, through the securities market. This "stock fever" has been exemplified on several occasions throughout China, where citizens have taken to the streets and rioted against police for the mere opportunity to engage in the securities market.²²² Hence, the Westernization of China's market-place appears to be inevitable.

If China seeks to experience continued economic growth into the 21st century, then it will have to open its market to the ideology of greater privatization and less government interference, and an economic structure in which the private sector, not the state, owns a majority interest in the country's enterprises. The implementation of these economic reforms will produce greater incentives for its people to pursue operational efficiency, while corporate management will incur a sense of accountability to the private sector for the profits and losses of their business. The government must also allow its debt and equities markets to be driven by a policy of laissez-faire, in which market forces determine the fate of the nation's enterprises and securities market, thereby producing a more efficient marketplace in China. If, however, the Party continues to pursue a policy of government interference, "then it will almost certainly guarantee the failure of the securities market in most respects, except of course, in the most short-term of objectives – capital infusion from the domestic and foreign shareholding public."223 Thus, to accomplish these ambitious goals, it will be necessary for China to improve upon its securities laws, for the purpose of creating an environment that encourages these capitalist theories.

The newly improved Securities Law must not only force the debt and equities market to become more dependent on market factors instead of state directives, but it must also implement measures to rectify the Chinese share structure and to ensure the equality of all shareholders – both foreign and domestic. Additionally, it must continue to put forward an environment

^{222.} See Chao, supra note 22, at 25.

^{223.} Cao, supra note 6, at 54.

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that encourages a process of takeovers and mergers. Furthermore, the Law must demonstrate China's resilience to prohibit fraudulent activities, such as insider trading and manipulation in the marketplace, and encourage the disclosure of trustworthy and accurate company information, as well as the free-flow of information from the financial media. Finally, it must recognize the benefits of a private shareholder litigation scheme, which has the function of supplementing the government's regulatory authorities in the enforcement of the Securities Law

However, with the implementation of these Western capitalist theories into the Chinese marketplace, the survival of the Party will be at stake. The inherent conflict of one country having two systems — a communist government with a capitalist securities market — will make it impossible for the current government to retain control over China. The Party has no real alternative but to support a securities market, as its failing state-run economy is in dire need of capital. Hence, it is inevitable that China's securities market will continue to æcend into a structure that is guided by market economics at the expense of its communist politics.

ALUMNI RESEARCH GUIDES

THE CASE OF GENERAL AUGUSTO PINOCHET: A LEGAL RESEARCH GUIDE

Kathleen M. Johnson*

I. Introduction

General Augusto Pinochet, dictator of Chile from 1973 to 1987, has repeatedly been accused of having committed innumerable atrocities against his political opponents during his time in office, both within Chile and abroad. As information about the internal workings of his police state was uncovered, certain key players in the international legal community paid close attention. When Hnochet was physically present in a country with which Spain had a formal extradition treaty, a Spanish magistrate sought his extradition to face charges in a Spanish court for the crimes he committed while in office. This Pathfinder provides a research framework for students, scholars and professors of law who are interested in the Pinochet case. This Pathfinder focuses on sources written in the English language.

Part II of this Pathfinder discusses the historical and procedural background of the Pinochet case. Part III identifies the key sources available to someone researching the Pinochet legal proceedings. Part IV describes useful finding tools.

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II. THE PINOCHET CASE

A. Historical Background

In September 1973, General Augusto Pinochet successfully led the Chilean military in a violent coup d'etat of a democratically elected government. He swiftly introduced the hallmarks of a police state to eliminate his political opposition. Most notably, he authorized the imprisonment, torture and execution of a large group of loosely defined "subversives."

Pinochet brutally repressed thousands of left-wing sympathizers. His victims included citizens of Chile, Spain and the United Kingdom.³ Pinochet then exported his terrorism across international borders through Operation Condor, "a plan of mutual cooperation among intelligence agencies of different South American countries."⁴ In 1987, Pinochet agreed to relinquish his position as head of state so long as he was able to remain head of the armed forces until 1998, at which time he was made a senator for life.⁵

B. Procedural Background

In 1996, a team of Spanish lawyers and magistrates, known as the Progressive Association of Prosecutors ("Association"), launched efforts to hold accountable the Argentinean and Chilean military officers who were responsible for numerous deaths and disappearances in the 1970's.⁶ Discovering that Pinochet was in London for medical reasons, the Association appealed to

^{1.} See Amnesty International USA, The Case of General Pinochet, at http://www.amnestyusa.org/countries/chile/pinochet_case.html (last visited Mar. 20, 2002).

^{2.} See Margarita Lacabe, Derechos Human Rights, The Criminal Procedures Against Chilean and Argentinean Repressors in Spain: A Short Summary, at http://www.derechos.net/marga/papers/spain.html (last visited Mar. 20, 2002) [hereinafter DHR Report].

^{3.} See Michael Byers, The Law and Politics of the Pinochet Case, 10 Duke J. Comp. & Int'l L. 415, 417 (2000).

^{4.} See DHR REPORT, supra note 2; Scott Armstrong & Saul Landau, Pinochet: Is a Terrorist Hiding in Chile's Senate?, at http://www.derechos.org/nizkor/chile/doc/armstrong.html (last visited Mar. 20, 2002).

^{5.} See DHR REPORT, supra note 2; Armstrong & Landau, supra note 4.

^{6.} See Mark Lakota, The Truth About Pinochet: Chile's Legacy of Torture, Murder, International Terrorism and "the Disappeared," at http://www.lakota.clara.net (last visited Mar. 20, 2002).

the British government to apprehend Pinochet for extradition. They invoked the European Convention on the Suppression of Terrorism,⁷ a mutually binding treaty obliging signatories to detain suspected international terrorists.

Pinochet was arrested in London on October 16, 1998.8 The arrest, however, was quickly ruled unlawful by the British Divisional Court on the grounds that, as a former head of state, Pinochet was immune from such prosecution in British courts.9 Despite this initial victory for Pinochet, the House of Lords ruled in later proceedings that Pinochet did not have immunity from prosecution. In October 1999, the Magistrates' Court ruled that Pinochet could be extradited to Spain to face charges. In

Pinochet then underwent a series of medical evaluations to determine whether he was mentally capable of standing trial. The medical reports concluded that he was not fit to face the charges against him.¹² British Home Secretary Jack Straw endorsed the reports, and received backing from the High Court when his decision was challenged.¹³ Pinochet left Britain on March 2, 2000, aboard a Chilean Air Force aircraft.¹⁴

Pinochet did not escape all charges against him; many plaintiffs lodged lawsuits against him in Chile, accusing him of torture and murder during his time in office. ¹⁵ After being placed under house arrest in January 2001, however, the Santiago

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^{7.} European Convention on the Suppression of Terrorism, Jan. 27, 1977, Europ. T.S. No. 90 [hereinafter Convention on Terrorism].

^{8.} See DHR REPORT, supra note 2.

^{9.} See Regina v. Bartle & Commissioner of Police for the Metropolis and Others, Ex Parte Pinochet, 37 I.L.M. 1302 (1998), available at http://www.derechos.net/doc/hl.html (last visited Mar. 20, 2002).

^{10.} See Regina v. Bartle & Commissioner of Police for the Metropolis and Others, Ex Parte Pinochet Ugarte (Amnesty International et al. intervening) (No. 3), 2 All E.R. 97 (H.L. 1999).

^{11.} See The Kingdom of Spain v. Augusto Pinochet Ugarte (Magistrates' Court 1999), available at http://www.open.gov.uk/lcd/magist/pinochet.htm (last visited Mar. 20, 2002).

^{12.} See Transnational Institute, Operation Exit: The Political Decision, Full Text of Jack Straw's Decision (Mar. 2, 2000), at http://www.tni.org/pinochet/docs/straw3.htm.

^{13.} See id.

^{14.} See Transnational Institute, Pinochet Case Timeline, at http://www.tni.org/pinochet/docs/timeline.htm (last visited Mar. 20, 2002).

^{15.} See id.

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Appeals Court reduced many of the charges. In July 2001, that same court decided to suspend the legal proceedings against Pinochet until further notice.

III. PINOCHET LEGAL RESOURCES

A. Pinochet for Beginners

For researchers not well-versed in Chilean political history, Pinochet's dictatorship, or the legal proceedings accusing the former dictator of crimes against humanity, visiting the followwebsite is a necessary first step: Sponsored by Electronic Telehttp://www.telegraph.co.uk. graph, a U.K. news channel, this site provides a thorough history of Chilean politics, and guides one through the key events leading up to Pinochet's 1998 arrest in London. It also offers a complete recapitulation of the legal proceedings since 1998, and is integral to an understanding of the Pinochet case. Prior to viewing most materials at this site, a researcher must complete a brief registration form.

B. Print Resources

1. International Treaties

To understand the international legal principles underlying the Pinochet case, one should review the relevant international treaties. The European Convention on the Suppression of Terrorism, to which both Spain and the U.K. are signatories, arguably provides the justification under international law for the actions taken by both countries. The 1957 European Convention on Extradition served as the basis for Spain's extradition request. Both are available in *International Legal Materials*, a bi-monthly publication compiling key international documents, as well as the *European Treaty Series*. These Conventions are also accessible through the fee-based United Nations Treaty Collection, http://untreaty.un.org.

^{16.} See Convention on Terrorism, supra note 7.

 $^{17.\} See$ European Convention on Extradition, Dec. 13, 1957, Europ. T.S. No. 24.

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2. Court Documents

While the Pinochet case directly involved Spain, Chile and the U.K., the key court decisions are those issued by the Chilean and British benches. Spain merely issued a request for extradition, while the U.K. courts exclusively dealt with the actual legal proceedings surrounding the request for extradition. Chilean prosecutors did not initiate proceedings against the former dictator until his return in March 2000, but were entertaining over one hundred criminal complaints against him by May 2000.

A highly authoritative court reporter for the British House of Lords is Law Reports, available in print at locations such as Brooklyn Law School Library and the New York University School of Law Library. All House of Lords decisions since November 1996 are conveniently available on the Internet at http://www.parliament.thestationeryoffice.co.uk/pa/ld199697/ldjudgmt/ldjudgmt.htm. Some key Pinochet proceedings took place in the lower courts, namely the Magistrates' Court and the Divisional Court. The texts of those decisions are also available online, on the Equipo Nizkor website discussed below. Regarding Chile, Revista de Derecho de Jurisprudencia y Gaceta de los Tribunales is available in print at Yale Law School Lillian Goldman Library.

3. Books

The Pinochet case is still rather recent. A researcher can review the works below and can use the finding tools described in Part IV of this guide to locate supplemental sources. *The Pinochet Case: A Legal and Constitutional Analysis*, is a compilation of writings by numerous authors edited by Diane Woodhouse and is available at the Brooklyn Law School Library. It is particularly helpful because it is one of the most up-to-date sources as of the publication of this guide. It provides not only a detailed calendar of events leading up to Pinochet's arrest, but also an in-depth analysis of the most important international legal issues, such as sovereign immunity and universal jurisdiction.

^{18.} THE PINOCHET CASE: A LEGAL AND CONSTITUTIONAL ANALYSIS (Diana Woodhouse ed., 2000).

When Tyrants Tremble: The Pinochet Case, 19 is written by Sebastian Brett and published by Human Rights Watch. This book provides helpful information and critical perspectives on the Pinochet case. Brett details the Chilean political history leading up to Pinochet's dictatorship, follows Pinochet through his fourteen years in office, and explains the implications of Spain's accusations. He then discusses the actual legal arguments entertained by the House of Lords in the proceedings. Finally, Brett concludes by addressing reactions in both Chile and the United States. Both the Arthur W. Diamond Law Library at Columbia Law School and the Fordham University Law Library own this title.

Another valuable work is *United Kingdom: The Pinochet Case: Universal Jurisdiction and the Absence of Immunity for Crimes Against Humanity*, ²⁰ published by Amnesty International. This title is highly technical in its legal discussion of Pinochet's dictatorship and thoroughly examines the Chilean constitution, relevant Chilean laws and the role of the Chilean military courts. It provides an exhaustive analysis of the applicable international legal principles, citing provisions of the key treaties along the way. It even offers a comprehensive history of the international jurisdictional principles at play. Explicitly limiting itself to only three of the topics argued in the Pinochet proceedings, this book is an essential resource for all researchers of this subject and is available at the St. John's University School of Law Library.

4. Periodicals

With minimal effort, any researcher may locate numerous helpful legal periodical articles discussing the Pinochet case. One thorough discussion appears in *The Law and Politics of the Pinochet Case*, 21 written by Michael Byers and published by the *Duke Journal of Comparative and International Law*. This piece is particularly helpful for researchers looking for a detailed discussion of the actual proceedings. Byers personalizes

^{19.} Sebastian Brett, When Tyrants Tremble: The Pinochet Case (1999).

^{20.} Amnesty Int'l, United Kingdom: The Pinochet Case: Universal Jurisdiction and the Absence of Immunity for Crimes Against Humanity (1999).

^{21.} Byers, supra note 3.

the key players by recounting the court room antics of the barristers and the judges.

For a slightly different angle on the Pinochet case, one will certainly want to read *Reflections on Pinochet*,²² written by Clive Nicholls, leading counsel for Pinochet in the British courts. He comprehensively explains why Pinochet was not able to be tried in the U.K. for the crimes Spain alleged against him. He also asserts that, had a suitable international criminal court existed at the time of the Pinochet proceedings, Pinochet would have stood trial and been held accountable for his actions as dictator. Nicholls' article was published by the *Virginia Journal of International Law*, and is available at most law school libraries.

Jurisdiction in the Pinochet Case: The View From Spain,²³ by Leslie Turano Taylor, provides an interesting and unique comparison of the Spanish Criminal Court's approach to the same issues that were before the House of Lords, namely terrorism, torture and jurisdiction. Taylor's article was published by European Public Law, which may be found in both Fordham University's and New York University's libraries.²⁴

C. Internet Resources

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The Internet provides an abundance of information on the Pinochet case and, due to the very nature of this tool, is more up-to-date than either the books or periodicals described previously.

Equipo Nizkor, a Spanish organization specializing in the promotion and awareness of human rights, sponsors an extremely useful website for purposes of Pinochet research. Iocated at http://www.derechos.org, this site is devoted to the human rights issues that underlie the Pinochet trial, particularly terrorism and persecution. Clicking on "Site Map" on the main page of the website leads one to a list of topics organized by category. The first category, "Human Rights Issues," offers a hyperlink to information on Pinochet. By clicking on this link,

^{22.} Clive Nicholls, Reflections on Pinochet, 41 VA. J. INT'L L. 140 (2000).

^{23.} Leslie Turano Taylor, *Jurisdiction in the Pinochet Case*, 6 Eur. Pub. L. 613 (2000).

^{24.} *Id.* Another equally informative article is Andrea Bianchi, *Immunity Versus Human Rights: The Pinochet Case*, 10 Eur. J. Int'l L. 237 (1999), available at Fordham University's and New York University's libraries.

a researcher will have immediate access to articles and publications on the Pinochet trial, as well as links to the actual British House of Lords documents. This website furnishes information in both English and Spanish. It also equips the researcher with links to rather obscure information, such as links to declassified U.S. government documents relating to the Chilean coup d'etat in the 1970's.

Another useful website is sponsored by Human Rights Watch, an organization with goals similar to that of Equipo Nizkor. Located at http://www.hrw.org, this website supplies the researcher with access to key articles on the Pinochet case. While it does not offer hyperlinks to the underlying British court decisions or international treaties, it does furnish the researcher with critical commentary on the Pinochet proceedings and will prove indispensable to those interested in learning more about Pinochet. One should go to the main webpage at the above address and click on "Campaigns." Clicking on "Americas" and again on "More News Releases" will lead a researcher to a link entitled "The Pinochet Decision," which contains the available Pinochet information on this site.

Amnesty International also provides a useful website, located at http://www.amnesty.org. By clicking on the "Search" option, and typing "Pinochet" into the query box, one will encounter a lengthy list of relevant articles published by this organization.

IV. DATABASES AND FINDING TOOLS

A. Library of Congress

The most appropriate Library of Congress subject heading to use for research purposes is "Pinochet Ugarte, Augusto." There are, however, several other subject terms that will prove useful to researchers looking for more obscure sources on this topic. "Criminal jurisdiction: Great Britain," "Extradition: Great Britain" and "Crimes against humanity: Chile" will all yield informative resources.

B. Reynolds and Flores

Thomas Reynolds and Arturo Flores, from the University of California, Berkeley, maintain a fee-based website that has proven to be an indispensable tool when conducting foreign le-

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gal research. Their online *Foreign Law Guide* provides extensive overviews of legal systems around the world.²⁵ Not only do they discuss the political histories of over 150 jurisdictions, but they also identify the official legal resources of each. For example, by clicking on "Chile" in the country menu on the left of the opening screen, one will encounter a brief but detailed summary of Chilean political history; one will also find the names of key court reports, as well as the names of major codifications. Reynolds and Flores will also direct the researcher to other helpful Internet sources.

C. Globalcourts Website

Through *Globalcourts.com*, Chief Judge Stein Schjølberg of Norway provides a useful and free Internet service for anyone researching court decisions of foreign jurisdictions. Located at http://www.globalcourts.com/decisions.htm, this site provides access to supreme court decisions from around the world. In most cases, the links will take a researcher directly to the official court website for a given jurisdiction.

D. First Search/World Cat

First Search, a fee-based database available at Brooklyn Law School Library, offers access to the World Cat online union catalog. A search on World Cat will provide a researcher with bibliographic information about books on a given topic and will direct the researcher to the libraries that carry those titles. By conducting an advanced search in World Cat, and limiting the search to titles that contain "Pinochet" and titles that are in the English language, the researcher will retrieve bibliographic information for ninety-six sources, as well as the location of each source. If one does not limit by language, a World Cat search by subject "Pinochet Ugarte, Augusto" produces 220 records. World Cat permits the researcher to view bibliographic records for the most recently published works first in the results list.

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^{25.} Brooklyn Law School Library has access through the use of a password obtainable at http://brkl.brooklaw.edu > "Online Subscription" > "Reynolds & Flores."

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E. Index Master

Index Master searches indexes and tables of contents to over 8,000 legal treatises. This finding tool is available at Brooklyn Law School Library. Recommended search terms are: "Pinochet," "extradition" and "sovereign immunity." Focus on recently published works.

F. Index to Foreign Legal Periodicals

The *Index to Foreign Legal Periodicals* provides citations to many international and comparative law periodical articles and is the "secret weapon" for foreign legal research. By looking in the subject index under the term "extradition," one will encounter a list of countries and the bibliographic information for relevant articles. In a recent issue, under the heading for Spain, the author found a reference to an article published by *Human Rights Quarterly, Prosecuting Rnochet: International Crimes in Spanish Domestic Law.*²⁶ Oddly enough, many of the other databases and finding tools will not direct the Pinochet researcher to this interesting article, which is why this index is so important.

G. Westlaw

Westlaw, a fee-based database located at http://westlaw.com, also proves extremely valuable to anyone researching this topic. Westlaw offers the Legal Journals Index ("LJI"), a database that indexes articles from legal journals published in the U.K. and Europe, covering over 430 English language journals since 1986. Many searches will provide only abstracts of full-length articles; however, this system allows a researcher to quickly identify the most useful articles and then focus on b-cating the journals that published them. Entering the LJI database and searching for "Pinochet" in the title and index fields retrieves a manageable thirty-nine abstracts. By conducting the same search in another database, Journals and Law Reviews Combined ("JLR"), a researcher will obtain full-text articles available through Westlaw, some of which are described

26. R.J. Wilson, Prosecuting Pinochet, International Crimes in Spanish Domestic Law, 21 Hum. Rts. Q. 927 (1999).

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above. JLR's coverage is not limited to European legal journals.

H. Public International Law: A Current Bibliography of Books and Articles

The online version of Public International Law: A Current *Bibliography* Booksand Articles. located of http://www.virtual-institute.de/en/hp/e-pil.cfm and sponsored by the Max-Planck Institute, is a valuable tool for locating books and articles. By clicking on "Online Documentation of Articles" on the opening page of the website, one will see a subject classification list. To identify a specific subject, a researcher can use the "find on this page" feature of one's web browser. The classification most appropriate for purposes of Pinochet research is "VR 18.5 - Extradition." After clicking on the "Extradition" hyperlink, one can peruse the bibliographic contents of over 100 titles. As of the publication of this guide, there were six titles devoted solely to the Pinochet case. There are semiannual updates to this bibliography.

V. Conclusion

This Pathfinder is intended to help both seasoned and beginner international researchers locate material on the Pinochet case. While the court decisions were handed down only a few years ago, they have already sparked an abundance of legal discourse on extradition and sovereign immunity. The sources in Part III detail the current situation, while the databases and finding tools in Part IV will help the Pinochet researcher locate future articles and books.

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A GUIDE TO RESEARCHING THE CARIBBEAN COURT OF JUSTICE

Rhea P. Hamilton*

I. Introduction

This Pathfinder outlines sources and techniques that are useful in researching the development of the Caribbean Court of Justice ("CCJ"). This guide also discusses research materials regarding Caribbean legal systems.

II. ESTABLISHING THE CARIBBEAN COURT OF JUSTICE

Currently, the Judicial Committee of the Privy Council in the United Kingdom serves as the ultimate arbiter of legal disputes that arise in most Member States of the Caribbean Community.¹ Guyana is an exception. Guyana abolished appeals to

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^{1.} See Hugh Rawlins, The Caribbean Court of Justice: The History AND ANALYSIS OF THE DEBATE 5 (2000), available at http://www.caricom.org (last visited Feb. 1, 2002); Roget V. Bryan, Comment, Toward the Development of a Caribbean Jurisprudence: The Case for Establishing a Caribbean Court of Appeal, 7 J. Transnat'l L. & Pol'y 181, 183 (1998). For further information on the appellate jurisdiction of the Judicial Committee of the Privy Council, see Privy Council Office, Judicial Committee, Judicial Committee of Council: Jurisdiction asatMarchhttp://www.privy-council.org.uk/judicial-committee/2000/jurisdiction.htm (last visited Feb. 1, 2002). Member States of the Caribbean Community include Antigua and Barbuda, The Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Haiti, Jamaica, Monserrat, St. Kitts and Nevis, St. Lucia, Suriname, St. Vincent & the Grenadines and Trinidad and Tobago. The Caribbean Community, Member Countries and Associated Members, at http://www.caricom.org (last visited Feb. 1, 2002).

the Judicial Committee in 1970, and maintains its own court of last resort 2

The Judicial Committee Act of 1833³ formally established the Judicial Committee of the Privy Council.⁴ The Judicial Committee's authority developed from "the prerogative right of the Sovereign as the fountain head of all justice to entertain appeals from the courts in her dominions." Since the middle of the 17th century, the Judicial Committee has served as a court to hear appeals from British territories overseas.⁶

Establishment of the CCJ will mark a departure from the British system and a turning point in Caribbean jurisprudence. In 1970, the Jamaican Delegation to an inter-governmental conference held in Jamaica recommended creation of a Caribbean Court of Appeal to replace the Judicial Committee of the Privy Council. The 2001 Agreement Establishing the Caribbean Court of Justice creates two distinct functions for the CCJ. First, the CCJ will have original jurisdiction when acting as an international tribunal to interpret and apply the Revised Treaty of Chaguaramas Establishing the Caribbean Community Including the CARICOM Single Market and Economy. Second, the CCJ will assume the jurisdiction of the Judicial Committee and will hear civil and criminal appeals from the lower courts of the Caribbean Community Member States. At a November 2001 meeting of the Legal Affairs Committee of

- 2. Bryan, supra note 1, at 183 n.8.
- 3. Judicial Committee Act, 1833, 3 & 4 Will. 4, c. 41 (Eng.).
- 4. RAWLINS, *supra* note 1, at 9, 20 n.5. Rawlins also identifies the English laws that further defined the Judicial Committee of the Privy Council. *See id.* at 20 n.8.
 - 5. 10 Halsbury's Laws of England ¶ 770 (4th ed. 1975).
 - 6. See RAWLINS, supra note 1, at 9; Bryan, supra note 1, at 183-84.
- 7. Duke Pollard, *The Caribbean Court of Justice: What It Is: What It Does* (Apr. 17, 2000), *at* http://www.caricom.org.
- 8. Agreement Establishing the Caribbean Court of Justice, Feb. 14, 2001, available at http://www.caricom.org > "Information Services" > "Treaties and Protocols" (last visited Feb. 1, 2002) [hereinafter Caribbean Court Agreement].
- 9. See Pollard, supra note 7. See also Caribbean Court Agreement, supra note 8, art. III and pt. II. Revised Treaty of Chaguaramas Establishing the Caribbean Community Including the CARICOM Single Market and Economy (2001), available at http://www.caricom.org > "Information Services" > "Treaties and Protocols" (last visited Feb. 1, 2002).
- $10.\ See$ Pollard, supra note 7. See also Caribbean Court Agreement, supra note 8, art. III and pt. II.

the Caribbean Community, participants noted that three jurisdictions must ratify the Agreement Establishing the Caribbean Court of Justice for this Agreement to enter into force; Barbados, Belize, Guyana, and Trinidad and Tobago expressed a willingness to promptly ratify the Agreement.¹¹

Proponents of the CCJ maintain that a court seated in the Caribbean and managed by judges from the region would have many benefits, such as achieving judicial independence for the Caribbean Community and issuing decisions that reflect the region's social standards. It could also bolster foreign investment if the CCJ decided cases in an expeditious manner.¹² Opponents of the CCJ cite concerns about funding; raise issues regarding the qualifications and impartiality of potential CCJ judges; and focus on potential human rights implications of CCJ decisions, particularly with respect to the death penalty.¹³

III. OBTAINING BACKGROUND INFORMATION ON CARIBBEAN LEGAL SYSTEMS

In an introduction to the Caribbean in their Foreign Law Guide, Thomas Reynolds and Arturo Flores note that a researcher will face severe problems in locating current laws of Caribbean nations.¹⁴ Reynolds and Flores describe Caribbean countries as "small jurisdictions lacking an audience of legal and judicial and business consumers sufficient to justify economic production of the most basic legal publications."¹⁵

There are, however, three valuable starting points exist to assist the researcher of Caribbean legal systems. Volume 7 of the *Modern Legal Systems Cyclopedia* focuses on the legal re-

^{11.} Press Release, Caribbean Community (CARICOM) Secretariat, Press Release Issued on the Conclusion of the Fifth Ordinary Meeting of the Legal Affairs Committee (LAC) of the Caribbean Community (CARICOM) Held in Port-of-Spain, Trinidad and Tobago, 28-30 November 2001, (Dec. 6, 2001), available at http://www.caricom.org > "Information Services" > "Press Releases" (last visited Feb. 1, 2002).

^{12.} See Pollard, supra note 7.

^{13.} Id.

^{14.} Thomas H. Reynolds & Arturo A. Flores, Foreign Law Guide: Current Sources of Codes and Basic Legislation in Jurisdictions of the World, The Caribbean: A Note About Its Development and Legislation, at http://www.foreignlawguide.com/FLG/frameset.htm (last visited Feb. 1, 2002) (subscription database available at Brooklyn Law School Library).

^{15.} *Id*.

gimes of Central America and the Caribbean. ¹⁶ It contains sections for each country of the Caribbean, including the subheading, "The Legal Systems of the Commonwealth Caribbean," which addresses the region as a whole. ¹⁷ "The Legal Systems of the Commonwealth Caribbean" is further divided into subsections: "Background"; "Sources of Law"; "Administration of Justice"; "Legal Education and Profession"; "Legal Materials"; "Legal Ethics"; and "Bibliography." This section was prepared by Velma Newton, Law Librarian, Faculty of Law Library, University of the West Indies, who has written extensively on Commonwealth Caribbean legal systems and sources.

Reynolds and Flores provide an overview of Caribbean legislation in their *Foreign Law Guide*. ¹⁹ The authors focus their discussion on organizations that have affected Caribbean legislation. The *Foreign Law Guide* overview also contains footnotes that cite to Caribbean law reporters and to two works by Velma Newton. Newton's two publications will be discussed later in this research Pathfinder. In other parts of the *Foreign Law Guide*, the authors describe key legislative publications and court reports of individual Caribbean jurisdictions.

The Common Law Abroad: Constitutional and Legal Legacy of the British Empire²⁰ is an extensive bibliography of sources regarding the colonial dependencies of Great Britain. It describes constitutional and legal works "generated in or for the British dependencies during the time of imperial influence, typically until independence."²¹ Author Jerry Dupont focuses on historical primary legal sources (excluding official gazettes) and selected secondary sources available in twelve major law libraries. This bibliography includes the sections "General Treatises"²² (excluding recently published treatises) and "British Caribbean."²³ For each geographic area in the "British Car

^{16. 7} MODERN LEGAL SYSTEMS CYCLOPEDIA (Kenneth Redden ed., 1984).

^{17.} See id.

^{18.} See id.

^{19.} Reynolds & Flores, *supra* note 14. Like the Modern Legal Systems Cyclopedia, the *Foreign Law Guide* also has separate sections for each Caribbean country.

^{20.} JERRY DUPONT, THE COMMON LAW ABROAD: CONSTITUTIONAL AND LEGAL LEGACY OF THE BRITISH EMPIRE (2001).

^{21.} Id. at viii.

^{22.} Id. at 1-42.

^{23.} Id. at 151-311.

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ibbean" section, Dupont includes citations to materials on the reception and administration of law.

To locate sources on the CCJ and Caribbean legal systems through many library catalogs, the researcher can employ the following Library of Congress subject headings:

- "Caribbean Area Politics and Government"
- "Appellate Courts Caribbean, English Speaking"
- "Courts of Last Resort Caribbean, English Speaking"
- "Jurisprudence Caribbean Region"
- "Law Caribbean Area"

"Law – Caribbean Area" is a particularly useful subject heading. Entering this subject search in law library catalogs will yield sources such as:

- Rose-Marie Belle Antoine, Commonwealth Caribbean Law and Legal Systems (1999). Antoine discusses legal systems, legal sources, courts and alternative dispute mechanisms in the Commonwealth Caribbean. This work includes the chapters "Introduction to Law and Legal Systems in the Commonwealth Caribbean," "The Reception of English Law and its Significance to Caribbean Jurisdictions" and "The Court System of the Commonwealth Caribbean." The chapter "The Caribbean Court of Justice and the Privy Council" is highly useful for the CCJ researcher.
- Albert Fiadjoe, Caribbean Public Law (1996). Fiadjoe notes that "the primary focus of this book is on the relationship between the courts and the executive branches of go vernment, and on the role of judicial review in the constitutional and go vernmental framework of the English-speaking Commonwealth Caribbean."²⁴ A second edition of this work, published in 1999, is now available.
- Velma Newton, Commonwealth Caribbean Legal Systems: A Study of Small Jurisdictions (1988). The content of this work mirrors that of Volume 7 of the Modern Legal Systems Cyclopedia, however, Commonwealth Caribbean Legal Systems provides more detailed treatment of Caribbean legal structures.
- Velma Newton, Commonwealth Caribbean Legal Literature: A Bibliography of All Primary Sources to Date and Secondary Sources for 1971-85 (1987). This contains information on

24. Albert Fiadjoe, Caribbean Public Law xi (1996).

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primary sources of law such as the constitutions and laws of Member States. It also includes data on many secondary resources such as periodicals, bibliographies, books and articles (including articles on the CCJ, referred to as the Caribbean Court of Appeal in this volume). The Faculty of Law Library, University of the West Indies, published this work. To update this *Bibliography*, the researcher might wish to contact staff of the Faculty of Law Library.²⁵

The researcher will also find useful materials through the following sources:

- World Cat on First Search, available at http://firstsearch.oclc.org. World Cat will enable the researcher to search library catalogs around the world. The author recommends searching this online union catalog because relevant titles on Caribbean law and the CCJ may not be available beally.
- WebLuis is the State University System of WebLuis.Florida's online union catalog. Research Analyst Andrew Zimmerman has described Florida State University at Tallahassee as the best American source of Caribbean legal materials.²⁶ The WebLuis subject query: "Law-Caribbean Area" produced thirty bibliographic records. A WebLuis search also yielded The Caribbean Journal of Legal Information, Caribbean Law and Business, Caribbean Law Bulletin and The Caribbean Law Review.²⁷ These legal periodicals will likely contain information on developments regarding the CCJ. To acuser friendly source, follow $_{
 m the}$ http://www.fsu.edu/~library > "WebLuis" > "SUS Library Catalogs and Course Reserve Indexes" > "Union Index to All Libraries." Enter search terms in the appropriate fields.
- The Libraries of the University of Puerto Rico. Also recommended by Zimmerman as a good source of Caribbean materials, ²⁸ one can access many of the libraries of the University of

^{25.} One could contact the Faculty of Law Library staff via email at lawlib@caribsurf.com or at pubserv@uwichill.edu.bb.

^{26.} Andrew Zimmerman, Zimmerman's Research Guide: Caribbean, at http://www.llrx.com/guide-gen/3/183.html (last visited Feb. 1, 2002).

^{27.} In the New York metropolitan area, Caribbean Law Bulletin, Caribbean Law Review and Contemporary Caribbean Legal Issues are available at the New York University School of Law Library (the JULIUS Online Catalog is available through http://julius.law.nyu.edu).

^{28.} Zimmerman, supra note 26.

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Puerto Rico at http://www.upr.clu.edu/upri > "On-line Libraries." Use the subject searches recommended previously to find numerous volumes on the Caribbean.

• Faculty of Law Library at the University of the West Indies, Cave Hill Campus. Though not equipped for online catalog searches, this library is a premier source of Caribbean legal materials. From *The Faculty of Law, University of the West Indies*, at http://law.uwichill.edu.bb, the researcher can browse the University's serial holdings and obtain other general library information. One could contact library staff via e-mail at lawlib@caribsurf.com or pubserv@uwichill.edu.bb.

IV. RESEARCHING THE CCJ

A. Website of the Caribbean Community (CARICOM) Secretariat

Once the researcher has acquired background information on Caribbean legal systems, the researcher can focus on the CCJ. The best starting point is the website of the Caribbean Community (CARICOM) Secretariat, at http://www.caricom.org, an up-to-date and authoritative source on the CCJ. Clicking on the site's "CCJ" link, the researcher will be able to review a great deal of information on the CCJ. This link is divided into thirteen subsections through which the researcher can obtain documents such as: Agreement Establishing the Caribbean Court of Justice; Agreement Establishing the Seat of the Caribbean Court of Justice and the Offices of the Regional Judicial and Legal Services Commission Between the Government of Trinidad and Tobago and the Caribbean Community; draft rules of the CCJ; the proposed Code of Judicial Conduct; and an overview of the CCJ organized in a question-and-answer format.

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B. Books and Papers on the Caribbean Court of Justice

In addition to Antoine's *Commonwealth Caribbean Law and Legal Systems*,²⁹ the researcher should also consult the following texts:³⁰

- Conference on Governance in the Contemporary Caribbean: The Way Forward: Selected Papers (2001).
- Hugh Rawlins, Caribbean Court of Justice: The History and Analysis of the Debate (2000).
- Caribbean Court of Justice: Critical Viewpoints from a Caribbean Rights Symposium (1998).
- Stephen Vasciannie, The Privy Council Versus the Caribbean Court of Appeal: Some General Observations (1996).

An "Advanced Search" query on World Cat employing the keyword phrases "Caribbean Court of Justice" and "Caribbean Court of Appeal" yielded these titles. Rawlins' paper is available through Caribbean Community (CARICOM) Secretariat at http://www.caricom.org > "CCJ." Vasciannie's work is available at Harvard Law School Library and Yale University Library.³¹ The other two sources are available in the collection of the University of the West Indies. Alternatively, the researcher can attempt to obtain Conference on Governance in the Contemporary Caribbean: The Way Forward: Selected Papers from the Caribbean Community (CARICOM) Secretariat, and Caribbean Court of Justice: Critical Viewpoints from a Caribbean Rights Symposium from the Caribbean Human Rights Network. The websites of both bodies have links through which one can order publications.³²

^{29.} Rose-Marie Belle Antoine, Commonwealth Caribbean Law and Legal Systems (1999).

^{30.} The author was unable to review some of these texts for the purposes of this guide. Generally, sources on Caribbean law and the CCJ published by the Caribbean Community (CARICOM) Secretariat and the University of the West Indies will be highly useful.

^{31.} The Harvard OnLine Library Information System, at http://hollisweb.harvard.edu (last visited Feb. 1, 2002); Yale University Iibrary, Orbis & Library Catalogs, at http://www.library.yale.edu/orbis (last visited Feb. 1, 2002).

^{32.} To order materials through the Caribbean Community (CARICOM) Secretariat's website, at http://www.caricom.org, click on the "Publications" link. For publications of the Caribbean Human Rights Network, send orders or inquiries via e-mail to crights@caribsurf.com, or call (246) 436–9456.

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C. Other CCJ Sources

1. Legal Periodical Articles

Since the CCJ is a developing institution, the researcher should consult current legal periodical articles about this court. *Westlaw* and *LexisNexis* provide databases in which to retrieve such articles.

Through Westlaw, at http://westlaw.com, the author conducted searches in three legal periodical databases. The *Legal* Resource Index database (coverage: 1980 - present) provides citations to articles from over 850 legal sources published in the United States, Canada, Great Britain, New Zealand and Australia. The *Legal Journals Index* database (coverage: 1986 - present) includes citations to journal articles published in the United Kingdom and Europe. The International Law - Law Reviews, Texts & Bar Journals database consists of documents from various secondary legal sources, including law reviews, texts, bar journals and legal-practice oriented materials. The author executed the following "Terms and Connectors" searches in these three databases: "ti, in(caribbean)" and "ti, in(caribbean court of justice)." Dianne Stafford's brief article, Caribbean Court of Justice, 33 provides a recent analysis of the CCJ. Roget Bryan's comment in the Journal of Transnational Law and Policy is highly useful because it outlines the history of the Judicial Committee of the Privy Council and the formation and development of the CCJ.³⁴

Through *LexisNexis*, at http://www.lexis.com, the researcher can retrieve full text legal periodical articles from the following path: "All Sources" > "Secondary Legal" > "Law Reviews, Combined." Recommended "Terms and Connectors" search queries are: "Title (caribbean) or Summary (caribbean);" "Title (caribbean court of justice) or Summary (caribbean court of justice);" and "Title (caribbean court of appeal) or Summary (caribbean court of appeal)." A key result is the article by Hugh A. Salmon titled *The Caribbean Court of Justice: A March With Destiny*. Moreover, one can obtain citations to articles and link to the

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^{33.} Dianne Stafford, Caribbean Court of Justice, 14 Com. Jud. J. 18 (2001).

^{34.} Bryan, supra note 1.

^{35.} Hugh A. Salmon, The Caribbean Court of Justice: A March With Destiny, 2 Fla. Coastal L.J. 231 (2000).

text of selected articles through the online *Legal Resource Index* (coverage: 1977 - present). Access *Legal Resource Index* through the path: "All Sources" > "Secondary Legal" > "Annotations & Indexes" > "Legal Resource Index."

The *Index to Foreign Legal Periodicals* ("IFLP") is a tool to locate scholarly articles and collections of essays. It includes citations to sources that are not available through either *Lexis Nexis* files or *Westlaw* databases. In the IFLP subject index, "Courts and Tribunals" and "Administration of Justice" are useful headings. The best way to use IFLP for CCJ research, however, is to consult the geographical index under the heading "Caribbean," particularly if journal title or author information is unavailable. The author reviewed the 1998-2000 volumes and 2001 issues of the IFLP. The following are two titles of potential relevance:

- Rosalea Hamilton, Stare Decisis and the Development of Caribbean Jurisprudence, 8 Caribbean L. Rev. 330 (1998); and
- Hugh A. Rawlins, State Proceedings in the Commonwealth Caribbean, 7 Caribbean L. Rev. 497 (1997).

2. News

News sources also report on recent activities concerning the CCJ. Both *LexisNexis* and *Westlaw* have rich news databases that will assist the researcher.

On LexisNexis, one can find news articles through the following path: "All Sources" > "News" > "Major World Newspapers." The Major World Newspapers file contains articles from over 140 newspapers from around the globe, many of which will cover CCJ developments. Westlaw enables the researcher to execute a region-specific search in the Latin America, West Indies and Caribbean News ("LATNEWS") database. LATNEWS offers materials from newspapers, magazines, transcripts, newsletters and news wires.

There are also many free Internet sources that contain news articles about the Caribbean region. Some noteworthy sites include *The Guyana Chronicle* at http://www.guyanachronicle.com, *The Barbados Nation Online* at http://www.nationnews.com, *The Trinidad Guardian* at http://www.guardian.co.tt and *Jamaica Gleaner* at http://www.jamaica-gleaner.com.

D. Other Internet Resources

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To locate additional Internet sites about the CCJ, the author recommends *Google*, at http://www.google.com, and an "Advanced Search" query using the phrase "Caribbean Court of Justice." Sites maintained by government bodies, bar associations, courts and law firms will likely contain reliable information. The following sites are helpful:

- The law firm of Myers, Fletcher & Gordon ("MFG") maintains a site at http://www.mfg-law.com. This site includes links to the firm's newsletter and to "Developments In West Indian Law." The June 2000 edition of the newsletter contains an article discussing the CCJ's power to resolve trade disputes between CARICOM nations. The author contacted this firm. In response, Derek Jones, a Partner at MFG and the President of the Jamaican Bar Association, provided two papers. These papers describe the history of the CCJ and discuss issues such as the cost of creating and maintaining the CCJ, questions of judicial impartiality, and suggestions for the CCJ's structure. These highly useful papers are: Position Paper of the Council of the Jamaican Bar Association on the Proposed Caribbean Supreme Court (March 16, 2000) and Presentation in Respect of the Proposed CCJ, presented in St. Lucia on August 16, 2000.
- The Supreme Court of Jamaica's website http://www.sc.gov.jm includes a "Caribbean Court of Justice" link. At this time, this link only transfers the researcher to the Ministry of National Security and Justice Jamaica at http://www.mnsj.gov.jm/caribCOA/index.htm ("Ministry"). The Ministry's site includes a summary document by Rosalea Hamilton, Legal and Economic Arguments in the Judicial Committee of the Privy Council v. Caribbean Court of Justice Debate (March 2000). The Ministry's site also provides articles in the online forum Caribbean Court of Justice Discussion Online. Additionally, the Supreme Court of Jamaica's website links to the Smithfield Digest, which contains notes and indexes of decisions from the courts of Jamaica and the Judicial Committee of the Privy Council.³⁶

36. Smithfield Digest, at http://www.Smithfield.com.jm (last visited Mar. 20, 2002).

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V. CONCLUSION

This guide highlights print and electronic sources on the CCJ and Caribbean law. Future actions of Caribbean Community Member States concerning the CCJ likely will result in publication of additional materials. The researcher will be able to locate such materials by visiting the website of the Caribbean Community (CARICOM) Secretariat at http://www.caricom.org and searching law library catalogs with the U.S. Library of Congress subject headings recommended in Part III of this guide. The researcher also will find current materials on the CCJ by using the database search queries and additional resources described in this Pathfinder.

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ANDREW P. VANCE MEMORIAL WRITING COMPETITION WINNERS

THE BEEF HORMONE DISPUTE AND CAROUSEL SANCTIONS: A ROUNDABOUT WAY OF FORCING COMPLIANCE WITH WORLD TRADE ORGANIZATION DECISIONS

Rosemary A. Ford*

"[T]he historian will see that trade was the principle of Liberty; that trade planted America and destroyed Feudalism; that it makes peace and keeps peace, and it will abolish slavery." 1

I. Introduction

A. Background

In 1989, the European Union ("EU")² imposed an absolute prohibition on the use of synthetic hormones that resulted in a ban of hormone-treated beef imported from the United States.³

^{*} J.D. (Candidate 2002), University of Pennsylvania Law School. The author wishes to thank Professor Curtis R. Reitz for his thoughtful advice.

^{1.} Ralph Waldo Emerson, The Young American, Lecture before the Mercantile Library Association (Feb. 7, 1844), in Nature: Addresses, and Lectures 302-03 (1895).

^{2.} The European Union was previously known as the European Community, and the World Trade Organization still uses that designation in its decisions. For the sake of clarity, the author has used EU throughout this paper except when referring to a World Trade Organization decision.

^{3.} For a brief chronology of the EU's Hormone Ban, see U.S. Dep't of Agric. Foreign Agric. Serv., FASonline, Chronology of the European Union's Hormone Ban, at http://www.fas.usda.gov/itp/policy/chronology.html (last visited Mar. 6, 2002).

In 1996, the U.S. appealed the ban⁴ following the dispute settlement procedure enacted along with the creation of the World Trade Organization ("WTO") in 1994.⁵ After an adverse panel decision⁶ had been appealed by the EU in 1997,⁷ the WTO appellate body issued a ruling against the EU that required it to lift the hormone ban in the absence of any scientific risk assessment of harm.⁸ A subsequent arbitral ruling authorized U.S. countermeasures against the EU for non-compliance with the decision within the fifteen-month accepted time period.⁹ The countermeasures took the form of 100% ad valorem¹⁰ U.S. tariffs on certain imports, up to an amount equivalent to the \$116.8 million of lost revenues that the arbitration panel determined the U.S. was losing annually as a re-

^{4.} See European Communities – Measures Concerning Meat and Meat Products (Hormones), Request for Consultations by the United States, WT/DS26/1, Doc. No. 96-0359 (Jan. 31, 1996), at http://www.wto.org/english/tratop_e/dispu_e/distabase_wto_members2_e.htm [hereinafter U.S. Request for Consultations].

^{5.} See Understanding on Rules and Procedures Concerning the Settlement of Disputes, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 2, Legal Instruments – Results of the Uruguay Round vol. 31, 33 I.L.M. 1226 (1994), available at http://www.wto.org/english/docs_e/legal_e/28-dsu.pdf [hereinafter DSU].

^{6.} See EC Measures Concerning Meat and Meat Products (Hormones), Complaint by the United States, Report of the Panel, WT/DS26/R/USA, Doc. No. 97-3368 (Aug. 18, 1997), at http://www.wto.org/english/tratop_e/dispu_e/distabase_wto_members2_e.htm [hereinafter WTO Panel Report].

^{7.} See EC Measures Concerning Meat and Meat Products (Hormones), Notification of an Appeal by the European Communities under Paragraph 4 of Article 16 of the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU), WT/DS26/9, Doc. No. 97-4084 (Sept. 25, 1997), at http://www.wto.org/english/tratop_e/dispu_e/distabase_wto_members2_e.htm.

^{8.} See EC Measures Concerning Meat and Meat Products (Hormones), AB-1997-4, Report of the Appellate Body, WT/DS26/AB/R, Doc. No. 98-0099 (Jan. 16, 1998), at http://www.wto.org/English/tratop_e/dispu_e/ distabase_wto_members2_e.htm [hereinafter WTO Appellate Body Report].

^{9.} EC Measures Concerning Meat and Meat Products (Hormones) – Arbitration Under Art. 21.3(c) of the Understanding on Rules and Procedures Governing the Settlement of Disputes, Award of the Arbitrator, WT/DS26/15, Doc. No. 98-2227, ¶ 48 (May 29, 1998), at http://www.wto.org/english/tratop_e/dispu_e/distabase_wto_members2_e.htm [hereinafter WTO Arbitrator Award].

^{10.} Meaning "according to the value" of the article, as opposed to by weight. Black's Law Dictionary 53 (7th ed. 1999).

sult of the ban.¹¹ Despite these legal rulings, the imposition of the tariffs and numerous trade negotiations, by the beginning of 2001 and the dawn of a new American administration, the European ban stood bloodied but unbowed, barring imports from the U.S. of high-grade, grain-finished beef.¹²

B. Causes of the U.S.-EU Standoff

The causes of this stalemate are varied. They include cultural and regulatory differences between the two entities, ¹³ as well as a possible agenda of protectionism. ¹⁴ In addition, the dispute has highlighted the difficulty of enforcing compliance with WTO rulings. In the now famous words of a former General Counsel to the Office of the United States Trade Represen-

- 11. European Communities-Measures Concerning Meat and Meat Products (Hormones), Original Complaint by the United States, Recourse to Arbitrations by the European Communities under Articles 22.6 of the DSU, Decision by the Arbitrators, WT/DS26/ARB, Doc. No. 99-2855, 83-84 (July 12, 1999), at http://www.wto.org/english/tratop_e/dispu_e/distbase_wto_members2_e.htm [hereinafter WTO Arbitrators Decision]. The U.S. claimed that actual losses ranged as high as \$500 million annually. George H. Rountree, Raging Hormones: A Discussion of the World Trade Organization's Decision in the European Union-United States Beef Dispute, 27 GA. J. INT'L & COMP. L. 607, 610 (1999).
- 12. The EU imported 21.3% of its 1998 merchandize from the U.S. NATO PARLIAMENTARY ASSEMBLY, COMMITTEE REPORTS, ECONOMIC AND SECURITY, GENERAL REPORT: THE WTO AND THE US-EUROPEAN ECONOMIC RELATIONSHIP (Nov. 2000), at http://www.nato-pa.int/publications/comrep/2000/at-253-e.html [hereinafter NATO REPORT].
- 13. Generally, EU food regulation is more supportive of traditional food processes that consumers and regulators believe is natural even in the face of scientific disapproval, and against food perceived as unnatural even in the face of scientific approval. See Marsha A. Echols, Food Safety Regulation in the European Union and the United States: Different Cultures, Different Laws, 4 Colum. J. Eur. L. 525, 525-29 (1998). For instance, European laws allow the production and consumption of raw milk cheeses and traditionally cured meats, which are considered unsafe for human consumption by the U.S. and many in the scientific community. See id. And, in contrast to the relative acceptance of genetically engineered products in the U.S., Europeans have called these organisms "novel foods," and demanded they be segregated and labeled. Id. See also John Stephen Fredland, Unlabel Their Frankenstein Foods!: Evaluating a U.S. Challenge to the European Commission's Labeling Requirements for Food Products Containing Genetically-Modified Organisms, 33 VAND. J. TRANSNAT'L L. 183, 184-85 (2000) (Genetically-modified agriculture and agricultural products are considered as "Frankenstein Foods" in Europe.).
 - 14. See discussion infra Part II.B.

tative ("USTR"), "the WTO has no jailhouse, no bail bond smen, no blue helmets, no truncheons or tear gas."¹⁵

The dispute over hormone-treated beef ("Beef Hormone")¹⁶ began in 1987, prior to the creation of the WTO, when the U.S. threatened to levy a 10% increase of duties on EU agricultural products¹⁷ pursuant to section 301 of the Trade Act of 1974.¹⁸ For a short period, the U.S. and EU were able to negotiate an "interim measure" that allowed for some import of U.S. beef in return for the lessening of section 301 tariffs.¹⁹ In 1989, the General Agreement of Trade and Tariffs ("GATT") council convened on the dispute, but discussions stalled.²⁰ Eventually, in 1996, two years after the establishment of the WTO, the U.S. requested a WTO consultation regarding the hormone ban.²¹ Under the WTO Dispute Settlement Understanding ("DSU"), the jewel in the crown of the Uruguay Round,²² "consultation" was the first part of a possible four-tier settlement process that the Beef Hormone dispute would test to its limits.²³

- 18. Trade Act of 1974 § 301, 19 U.S.C. § 2411 (2000).
- 19. McNiel, supra note 17, at 110-11.
- 20. See id. at 109-110.
- 21. U.S. Request for Consultations, *supra* note 4. *See also* Rountree, *su-pra* note 11, at 612.

^{15.} Judith Hippler Bello, *The WTO Settlement Understanding: Less is More*, 90 Am. J. INT'L L. 416, 417 (1996).

^{16.} The WTO refers to the case as "EC Measures Concerning Meat and Meat Products (Hormones)." *See, e.g., supra* notes 4, 6-9 & 11. The author shall use the term "Beef Hormone" when referring to the dispute.

^{17.} Dale E. McNiel, The First Case Under the WTO's Sanitary and Phytosanitary Agreement: The European Union's Hormone Ban, 39 VA. J. INT'L L. 89, 110 (1999).

^{22.} The Congress had made an effective DSU a principal goal of the U.S. negotiations during the Uruguay Round talks. Important changes from the previous GATT dispute system included: (1) time limits for each stage of the settlement process; (2) creation of an appellate body; (3) no requirement for consensus in the adoption of decisions; and (4) automatic authorization for countermeasures. Office of the U.S. Trade Representative, Executive Office of the President, The Uruguay Round Agreement Act, Statement of Administrative Action, Understanding on Rules and Procedures Governing the Settlement of Disputes (Sep. 27, 1994), at 1994 WL 761797 [hereinafter SAA].

^{23.} The four stages are: (1) consultations; (2) panel; (3) appellate body; and (4) arbitration. See generally DSU, supra note 5; WTO, Trading into the Future: Introduction to the WTO Settling Disputes, The Panel Process, at http://www.wto.org/english/thewto_e/whatis_e/tif_e/disp2_e.htm (last visited Feb. 22, 2002).

In May 2000, wearied by the ineffectiveness of the WTO-sanctioned tariffs and concerned about its domestic cattle industry, the U.S. came up with a new twist on an old solution. Section 301 of the Trade Act of 1974, the old solution, gave the President discretionary authority to impose retaliatory measures against any foreign government, act, policy or practice that "burdens or restricts United States commerce," and violates international obligations.²⁴ Section 407 of the Trade and Development Act of 2000, signed into law by President Clinton on May 18, 2000, added new bite to the so-called section 301 sanctions by allowing the U.S. to rotate the list of products targeted for tariffs every six months.²⁵

The EU protested these "carousel" sanctions, arguing they are illegal under WTO rules, and immediately filed a complaint with the WTO.²⁶ The EU and U.S. participated in the initial consultation stage of WTO dispute settlement in July 2000.²⁷ According to a USTR official, these talks were "formalistic," and not significant.²⁸ To date, the U.S. has failed to implement the rotation. British Prime Minister Blair was apparently able to halt implementation in September 2000 when he expressed concern over the possible demise of the Scottish cashmere industry as a result of the proposed new tariffs.²⁹ The U.S. had also been negotiating with the EU concerning its preferential tax treatment for foreign sales corporations,³⁰ and may have

^{24.} Trade Act of 1974 § 301, 19 U.S.C § 2411(a)-(b) (2000).

Trade and Development Act of 2000, Pub. L. No. 106-200, § 407, 114
 Stat. 251, 293-94.

^{26.} See United States – Section 306 of the Trade Act of 1974 and Amendments Thereto, Request for Consultations by the European Communities, WT/DS200/1, Doc. No. 00-2304 (June 13, 2000), at http://www.wto.org/english/tratop_e/dispu_e/distabase_wto_members4_e.htm [hereinafter EU Request for Consultations].

^{27.} Ian Elliott, European Trade Commissioner Pascal Lamy; United States Trade Standards, Compliance, FEEDSTUFFS, July 17, 2000, at 2.

^{28.} Off-the-Record Telephone Interview with Unnamed Official at the Office of the United States Trade Representative (Jan. 30, 2001) [hereinafter Telephone Interview].

^{29.} See Larry Elliott et al., Blair Warns U.S. of Trade War, GUARDIAN UNLIMITED (Sept. 7, 2000), at http://www.guardian.co.uk/Archive.

^{30.} See Patrick Tracey, Agriculture: Subsidies to EU Farmers to be Phased Out Over Next Decade, Trade Commissioner Says, INT'L TRADE DAILY, Jan. 5, 2001, at WL 1/5/2001 BTD d5. In February 2002, the WTO found for the EU in this dispute with the U.S. See Daniel Pruzin, Steel: WTO Members to Meet

wanted to strengthen its negotiating position by withholding sanctions the EU perceives as controversial.³¹

A new administration, lacking a negotiating history, may, however, be less interested in preserving imports of luxury woolen goods at the expense of the American cattle industry, which has been the largest single U.S. agricultural sector for the past forty years.³² For the last five years, despite its extraordinary competitiveness, domestic cattle industry has been in a state of crisis due to plunging cattle prices.³³ One way to help the downturn is to increase the volume of beef exports, but figures show that the U.S. beef and cattle market is already disproportionately liberalized compared to other countries.³⁴ Furthermore, although the \$116.8 million estimated by the WTO arbitration panel³⁵ may not seem significant in comparison with overall trading figures in the billions of dollars, this 1996 number in no way reflects the potential exports in a freetrade market to the largest import bloc in today's global economy. Carousel sanctions may open this market, and USTR Robert B. Zoellick has indicated that he thinks carousel legislation is a "powerful tool" for bringing the EU into compliance with international trading rules.³⁶

Informally to Sift Legal Responses to U.S. Steel Safeguards, Int'l Trade Daily (BNA) (Mar. 13, 2002), at WL 3/13/2002 BTD d3.

^{31.} See Daniel Pruzin, European Union: EU Initiates WTO Complaint to Derail U.S. 'Carousel' Retaliation as Unilateral, Int'l Trade Daily (BNA) (Jun. 7, 2000), at WL 6/7/2000 BTD d9.

^{32.} The cattle industry has generated more than \$30 billion in revenues for the last dozen years. See Terence P. Stewart et al., Trade and Cattle: How the System is Failing an Industry in Crisis, 9 MINN. J. GLOBAL TRADE 449, 452 (2000). For more information see U.S. Department of Agriculture, Economic Research Service, at http://www.ers.usda.gov/Briefing/FarmIncome.

^{33.} See Stewart, supra note 32, at 452.

^{34.} For instance, in 1997, the U.S. was the leading importer of beef in the world with a forecast of 1.034 million metric tons ("MT") while the more populous EU imported only 380,000 MT, and exported 910,000 MT. *See id.* at 492-93.

^{35.} See id. at 501.

^{36.} See Gary G. Yerkey, Trade Policy: U.S. Will Reassert Leadership on Trade, Pushing EU and Japan Aside, Zoellick Says, Int'l Trade Daily (BNA) (Jan. 31, 2001), at WL 1/31/2001 BTD d2.

C. Summary

This Note will argue that carousel sanctions may offer an attractive short-term political gain when applied to a dispute, such as Beef Hormone that has run on for fifteen years without a good faith resolution. Although the sanctions are trade restrictive, the U.S. leads the world in its lack of trade barriers, and perhaps can be forgiven for sparing use of this effective tool. Because of its disproportionate trade liberalization, the two-edged nature of sanctions is especially harmful to the U.S., harming the importer as well as the exporter. Carousel rotation, however, means that importers only stay on the target list for six months, thus redistributing the harm in such a way that its impact is individually lessened, though affecting more businesses. Ultimately, however, this Note argues that sanctions are not in the U.S.'s best interest since their trade-restrictive nature undermines this country's long and ardent dedication to the principles of free trade.³⁷ In addition, even if, carousel retaliation is conceded to be permissible under international law, which is not yet clear, sanctions have alienated private businesses on both sides of the Atlantic.³⁸ Finally, the WTO is slowly moving beyond the bilateral trade concessions that inspired the signatories of GATT.³⁹ The multilateral standards represented by, for instance, the Agreement on the Application of Sanitary and Phytosanitary Measures ("SPS Agreement") indicate a new legal departure for the WTO.40 Multilateral standards could imply multilateral enforcement, replacing the

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^{37.} See Terry L. Anderson & J. Bishop Grewell, It Isn't Easy Being Green: Environmental Policy Implications for Foreign Policy, International Law, and Sovereignty, 2 Chi. J. Int'l L. 427, 438 (2001).

^{38.} See, e.g., Gary G. Yerkey, European Union: Corporate Leaders Say U.S.-EU Disputes Harming Business, Urge Quick Resolution, INT'L TRADE DAILY (BNA) (Nov. 21, 2000), at WL 11/21/2000 BTD d12 ("These disputes feed protectionist sentiment that gives rise to calls for retaliation which can only have a negative impact on the business community.").

^{39.} See WTO, Understanding the WTO Agreement on Sanitary and Phytosanitary Measures (1998), at http://www.wto.org/english/tratop_e/sps e/spsund e.htm (last visited Mar. 5, 2002).

^{40.} Agreement on the Application of Sanitary and Phytosanitary Measures, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, Legal Instruments – Results of the Uruguay Round vol. 1, available at http://www.wto.org/english/doc_e/legal_e/15-sps.pdf (last visited Feb. 23, 2002) [hereinafter SPS Agreement].

bilateral sanctions employed to this point. This is the future toward which the U.S. must look even if it recognizes the need for at least the credible threat of sanctions in the interim.

In Section II, this Note will trace the history of the Beef Hormone dispute through the dispute settlement process of the WTO. This will include relevant social and political background to the dispute. Section III will discuss the legality and effectiveness of trade sanctions in general, and as a way of forcing compliance with WTO decisions. Section IV suggests alternate ways of enforcing compliance with WTO rulings that strengthen the goals of global free trade.

II. THE BEEF HORMONE DISPUTE

A. Scientific Background

Beginning in the 1950's, the U.S. Food and Drug Administration ("FDA") and the Department of Agriculture ("USDA") approved the use of endogenous and synthetic bovine growth hormones ("BGHs")⁴¹ as a safe, cost-effective way to increase the feed efficiency in grain-fed cattle.⁴² The cattle receive the hormones in the form of implants the size of pencil erasers behind their ears.⁴³ They are then able to convert the grain, usually corn, with greater rapidity into the succulent, high grade "marbled" meat that U.S. consumers enjoy.⁴⁴ Most of the beef exported from the U.S. is this choice cut variety.⁴⁵ BGHs were widely adopted in the U.S. because of the competitive advantage they gave to feedlots operating on razor-thin, even nega-

^{41.} The bodies of both humans and bovines produce three hormones in a *natural*, or endogenous manner as opposed to synthetic hormones that are manufactured. The latter have a slightly different molecular structure, but otherwise mimic the function of endogenous hormones. *See* McNiel, *supra* note 17, at 97.

^{42.} See id. at 99-100.

^{43.} Beef Hormones, CARGILL BULL. (Oct. 1996), at http://www.cargill.com/today/bulletin/t101996.htm.

^{44.} Beef with fat deposits within the muscle tissue (marbling) is more palatable to most people than lean beef without fat deposits. Marbling is most easily produced by feeding grain to the growing/fattening animals. *See* Rountree, *supra* note 11, at 607.

^{45.} See U.S. Department of Agriculture, Economic Research Service, at http://www.ers.usda.gov/Briefing/cattle/Trade.htm (last visited Feb. 25, 2002).

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tive profit margins.⁴⁶ By contrast, in countries with minimal demand, or a lack of financial resources to support demand for fatty meat, cattle can be grazed without expensive grain feedings and the resultant economic desirability of BGHs.⁴⁷

B. Political Reaction in Europe to Growth-Promoting Hormones

Prior to 1981, European countries followed differing policies on growth hormones.⁴⁸ In 1981, reports alleging that Italian children had grown enlarged breasts after eating imported baby food containing veal treated with diethylistilbestrol ("DES")⁴⁹ prompted an Italian boycott of veal imports from countries where the hormones were allowed.⁵⁰ In response to popular concern, the Council of the European Communities ("Council") passed Directive 81/602,⁵¹ forbidding the marketing of any new hormones pending further studies.⁵² Following the Directive, the EU established a Scientific Working Group ("Scientific Working Group") composed of twenty-two prominent European scientists to determine if the use of natural and synthetic growth hormones in animals had any scientifically observable effects on human health.⁵³ A year later, in 1982, the Scientific Working Group issued an interim report stating that it found no harm derived from the use of endogenous hor-

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^{46.} See Rountree, supra note 11, at 608.

^{47.} See id.

^{48.} See McNiel, supra note 17, at 100-01 (stating that prior to 1981, Italy, Denmark, the Netherlands, West Germany and Belgium had either banned or severely restricted use of the growth hormones whereas France, the United Kingdom, Ireland and Luxembourg licensed some hormone products).

⁴⁹. In 1954, DES was approved by the FDA for use in beef cattle but was later found to be a carcinogen and banned in the U.S. in the late 1970's. *Id.* at 99.

^{50.} *Id.* at 101.

^{51.} Council Directive 81/602, Concerning the Prohibition of Certain Substances Having a Hormonal Action and of Any Substances Having a Thyrostatic Action, 1981 O.J. (L 222) 32.

^{52.} This meant that in some EU Member States all but one of the hormones allowed in the U.S. were permissible. *See* McNiel, *supra* note 17, at 102

^{53.} The Scientific Working Group on Anabolic Agents in Animal Production, also known as the Lamming Committee, was chaired by Professor G.E. Lamming. See id.

mones.⁵⁴ With regard to synthetic hormones, the Scientific Working Group reported that it needed more data.⁵⁵

Despite the interim report, in 1985, the European Parliament ("Parliament") adopted a resolution stating that information regarding endogenous and synthetic hormones was "far from complete."56 It also noted that an "over production of meat and meat products . . . adds considerably to the cost of CAP [the EU's Common Agricultural Policy]."57 The European resolution occurred in the context of the introduction of milk quotas the previous year that had led to an increase of dairy cattle slaughtered for meat, more than doubling EU intervention stocks of beef.⁵⁸ Following the adoption of this resolution, a scheduled meeting of the Scientific Working Group was canceled, and on December 31, 1985, the EU banned the use of endogenous hormones with an exception for therapeutic and zootechnical purposes, and placed a complete ban on all synthetic hormones.⁵⁹ Member States were given a transition period of three years to bring their laws into compliance.⁶⁰ Two years later, in August 1987, the members of the Scientific

[T]hat the use of oestradiol 17- β , testosterone and progesterone [i.e. endogenous hormones] and those derivatives which readily yield the parent compound on hydrolysis after absorption from the site of application, would not present any harmful effects to the health of the consumer when used under the appropriate conditions as growth promoters in farm animals.

Id.

^{54.} See Communication from the Commission to the Council Concerning the Use of Certain Substances Having a Hormonal Action in Animal Production: Proposal for a Council Directive Amending Directive 81/602 Concerning the Prohibition of Certain Substances Having a Hormonal Action and of Any Substances Having a Thyrostatic Action, COM(84)295 final at 2. The Scientific Working Group found:

^{55.} See id.

^{56.} Resolution Closing the Procedure for Consultation of the European Parliament on the Proposal from the Commission of the European Communities to the Council for a Directive Amending Directive 81/602 Concerning the Prohibition of Certain Substances Having a Hormonal Action and of Any Substances Having a Thyrostatic Action, 1985 O.J. (C 288) 158, 158.

^{57.} Id.

^{58.} *See* McNiel, *supra* note 17, at 104 n.98.

^{59.} Id. at 104.

^{60.} See Council Decision 87/561 on Transitional Measures Concerning the Prohibition on Administration to Farm Animals of Certain Substances Having a Hormonal Action, 1987 O.J. (L 339) 70.

Working Group publicized what would become their final report, concluding that the synthetic hormones they studied were safe when used to promote growth.⁶¹

C. Other Influences on European Thinking

In 1984, scholars introduced the "precautionary principle" into international discourse in the First International Conference on the Protection of the North Sea.⁶² This controversial doctrine is still evolving, but, generally, it states that in the face of uncertainty and ignorance of effects, as in the case of possible marine pollution, science can inform decision-making. but ethical and political considerations are primary. 63 The EU has subsequently incorporated it into environmental policy, 64 advancing the principle as an international environmental doctrine.65 The EU is currently using it to require labeling for genetically modified products.⁶⁶ In defending the Council Directive banning the use of endogenous and synthetic growth hormones against various legal challenges, the Court of Justice of the European Communities ("ECJ") appeared to be applying precautionary principles. It found that the ban need not be based on scientific data alone, and that it was permissible to respond to political concerns expressed by the Parliament and the "anxieties and expectations" of consumers. 67

^{61.} See Ban on Growth Hormone 'Political,' Scientists Say, Montreal Gazette, Aug. 19, 1987, at A4.

^{62.} JOEL TICKNER ET AL., THE PRECAUTIONARY PRINCIPLE IN ACTION: A HANDBOOK 2 (1999), available at http://www.biotech-info.net/handbook.pdf (last visited Feb. 24, 2002).

^{63.} See id.

^{64.} See Article 174 of the Treaty Establishing the European Community has a requirement to base "Community policy on the environment . . . on the precautionary principle and on the principle that preventive action should be taken." Treaty Establishing the European Community, Nov. 10, 1997, art. 174, O.J. (C 340) 3, 254-55 (1997).

^{65.} See Rio Declaration on Environment and Development, June 14, 1992, U.N. Doc. A/CONF.151/5/Rev.1, 31 I.L.M. 874 (1992).

^{66.} See Echols, supra note 13, at 538.

^{67.} Case C-331/88, The Queen v. Minister for Agriculture, Fisheries and Food and the Secretary of State for Health *ex parte*: Fedesa and Others, 1990-10 E.C.R. I-4023, 4061-62, ¶¶ 7-10 (1990).

In 1986, bovine spongiform encephalopathy ("BSE"), or "mad cow disease" was detected in the United Kingdom.⁶⁸ Protein supplements containing contaminated sheep and cattle offal thought to cause the disease were forbidden in 1988, but the regulation was not strictly enforced until 1991-92.⁶⁹ By then, the disease had reached epidemic proportions, bringing output of the British beef industry to its lowest level in twenty years.⁷⁰ Despite extraordinary, and until recently successful, EU efforts to contain the outbreak,⁷¹ the public loss of confidence in food safety continues to color European attitudes.⁷² The recent outbreak of foot and mouth disease in the United Kingdom⁷³ will not help to change these attitudes.

D. The EU Hormone Ban Finds No Support in Science-Based Risk Assessments

In 1987, the Joint FAO/WHO Expert Committee on Food Additives ("JECFA")⁷⁴ found no harm in the use of endogenous

- 70. Ellen Ruppel Shell, Could Mad-Cow Disease Happen Here?, ATLANTIC MONTHLY, Sept. 1998, at 92, 92.
- 71. See Michael D. Lemonick, Can It Happen Here?, TIME, Jan. 29, 2001, at 58 (reporting recent outbreaks of the disease in Italy, Spain and Germany, along with deaths in France and Ireland).
- 72. The trust that U.S. citizens place in the FDA is not shared by European citizens whose governments and scientists have exposed them to BSE, dioxin contaminated food and gene-altered maize that killed butterflies. See, e.g., Ernst-Ulrich Petersmann, Prevention and Settlement of International Trade Disputes Between the European Union and the United States, 8 Tul. J. Int'l & Comp. L. 233, 252 (2000).
- 73. See, e.g., Sarah Lyall, Foot-and-Mouth Disease Intrudes, Putting British Farmers in Dread, N.Y. Times, Mar. 3, 2001, at A1.
- 74. JECFA is a committee of the Codex Alimentarius Commission, a joint endeavor of the Food and Agricultural Organization ("FAO") and the World Health Organization ("WHO"), that provides influential guidelines concerning food safety. The JECFA committee is an independent group of international experts that focuses on the scientific evaluation of a veterinary drug and does not consider government policies and politics. JECFA recommends an acceptable daily intake and a maximum residue limit for a veterinary drug residue in a specific food commodity. See Joint FAO/WHO Expert Committee on Food Additives, Fact Sheet, at http://www.fao.org/es/esn/Jefca/what-e.pdf (last visited Feb. 24, 2002).

^{68.} See Sean Henahan, Mad Cow Disease: The BSE Epidemic in Great Britain, An Interview With Dr. Frederick A. Murphy, Access Excellence, at http://www.accessexcellence.org/WN/NM/madcow96.html (last visited Mar. 6, 2002).

^{69.} See id.

hormones, and established acceptable daily intake levels and maximum residue limits for two synthetic growth hormones.⁷⁵ In a July 1991 meeting, the Codex Alimentarius Commission ("Codex"), whose standards guide the WTO in its decisions, after much discussion, decided against adoption of the acceptable daily intake limits prescribed by JECFA⁷⁶ in a decision that was primarily seen as political.⁷⁷ In 1995, again after much discussion,⁷⁸ Codex adopted the JECFA recommendations concerning the use of endogenous hormones and the intake levels for the two synthetic hormones.⁷⁹

In 1994, the SPS Agreement⁸⁰ was signed into law by 135 member countries as part of the Final Act of the 1984-1994 Uruguay Round re-negotiating the GATT.⁸¹ The SPS Agreement recognized the sovereign right of nations to take measures that affect food safety and animal and plant health, but stated that regulation shall not "arbitrarily or unjustifiably" discriminate.⁸² It also stated that regulatory measures should be based on a scientific risk assessment.⁸³ In drafting the SPS agreement to include a science-based risk assessment, negotiators "looked at the EU ban on imports of beef produced from

^{75.} See Joint FAO/WHO Expert Comm. on Food Additives, Evaluation of Certain Veterinary Drug Residues in Food: Thirty-Second Report (1988).

^{76.} See Codex Alimentarius Comm'n, Report of the Twenty-First Session of the Joint FAO/WHO Codex Alimimentarius Commission, Alinorm 95/37 (1995) [hereinafter Codex Report]. See also McNiel, supra note 17, at 108.

^{77.} See McNiel, supra note 17, at 108.

^{78.} See id. at 109.

^{79.} See Codex Report, supra note 76.

^{80.} SPS Agreement, *supra* note 40, at Annex A, \P 1(b) (defining a sanitary or phytosanitary measure as one applied "to protect human or animal life or health within the territory of the Member from risks arising from additives, contaminants, toxins or disease-causing organisms in foods, beverages or feedstuffs").

^{81.} Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations, Apr. 15, 1994, Legal Instruments-Results of the Uruguay Round vol. 1, 33 I.L.M. 1125 (1994) [hereinafter Final Act]. For the Final Act documents, see WTO, Legal Texts: The WTO Agreements, at http://www.wto.org/english/docs_e/legal_e/final_e.htm (last visited Mar. 5, 2002).

^{82.} See SPS Agreement, supra note 40, art. 5, \P 5.

^{83.} See $id. \ \ 2$.

cattle administered growth hormones as a prototypical example."84

E. The WTO Beef Hormone Decisions

1. The Panel Decision: A Victory for the U.S.

In April 1996, after consultations proved unfruitful, the Beef Hormone dispute went before a WTO panel.85 The panel determined that the SPS Agreement governed the dispute86 and that the ban was inconsistent with Articles 3.1, 5.1 and 5.5 of the Agreement.⁸⁷ Oddly, the panel did not look at Article 2, arguably the heart of the SPS Agreement, which states that measures can only be maintained with sufficient scientific evidence.88 Instead, it looked to Article 3.1 which imposes the obligation on states to "base their sanitary and phytosanitary measures on international standards . . . where they exist."89 The panel found a violation of this provision because the EU standard was not based on existing Codex standards.90 Article 5.1 mandates that SPS measures must be based on an assessment of the "risks to human . . . life or health . . . as appropriate to the circumstances."91 The panel determined that the EU did not have a scientific justification for going beyond international standards in instituting the hormone ban.⁹² Article 5.5 states that parties should avoid "arbitrary or unjustifiable distinctions" in levels of protection if the measures then result in "discrimination or disguised restriction of international trade."93 The panel found a violation based on the difference between the extreme level of protection for added hormones when compared with the lack of protection for these hormones as they occur naturally in foods, such as meat and dairy prod-

^{84.} See McNiel, supra note 17, at 90-91.

^{85.} See WTO Panel Report, supra note 6.

^{86.} For a discussion of whether hormonal substances naturally found in meat should be called "contaminants," see McNiel, *supra* note 17, at 114.

^{87.} See WTO Panel Report, supra note 6, \P 8.271.

^{88.} For a discussion of this issue, see McNiel, *supra* note 17, at 118-20.

^{89.} See SPS Agreement, supra note 40, art. 3, ¶ 1.

^{90.} See WTO Panel Report, supra note 6, \P 8.77.

^{91.} See SPS Agreement, supra note 40, art. 5, ¶ 1.

^{92.} See WTO Panel Report, supra note 6, \P 8.137.

^{93.} See SPS Agreement, supra note 40, art. 5, \P 5.

ucts,⁹⁴ or compared with the unlimited residue levels allowed for carbadox (a genotoxic substance) when used for growth promotion.⁹⁵

2. The Appellate Body Ruling Narrows the Scope of the Panel Findings

The EU appealed the decision to the WTO Appellate Body ("Appellate Body") which overruled the panel's findings with regard to Articles 3.1% and 5.5 of the SPS Agreement, but affirmed the holding that the EU had not based its regulation on a scientific risk assessment, and thus violating Article 5.1.97 It was a Pyrrhic victory for the U.S. Some commentators felt that the ruling weakened the SPS Agreement, demonstrating its inability to deal with complicated global issues.98 The Appellate Body's rejection of the Codex standards certainly represented a step backward in the process of harmonizing standards.⁹⁹ Further, it overruled the requirement that the æsessment had to be concluded at the time the measure was implemented. 100 This left open the door to a scientific finding by any scientist, orthodox or otherwise, that could provide the basis for a permissible risk assessment as the Appellate Body found that an SPS measure could derive from "a divergent opinion coming from qualified and respected sources," rather than exclusive reliance on "mainstream" scientific opinion. 101

In addition, the SPS Agreement lists a number of factors to be taken into account when conducting a risk assessment.¹⁰²

^{94.} See WTO Panel Report, supra note 6, ¶¶ 8.216, 8.241 & 8.271.

^{95.} See id. ¶¶ 8.197, 8.214 & 8.228.

^{96.} See WTO Appellate Body Report, supra note 8, ¶ 165 (stating that the SPS Agreement, although envisioning harmonization of standards in the future, does not require that recommendations, such as the Codex guidelines, be transformed into "binding norms").

^{97.} See id. ¶ 197 n.120.

^{98.} See Regine Neugebauer, Fine-Tuning WTO Jurisprudence and the SPS Agreement: Lessons from the Beef Hormone Case, 31 LAW & POL'Y INT'L BUS. 1255, 1256 (2000).

^{99.} See, e.g., McNiel, supra note 17, at 133.

^{100.} See WTO Appellate Body Report, supra note 8, ¶ 189 (What was required was an "objective situation that persists and is observable between an SPS measure and a risk assessment.").

^{101.} See id. ¶ 194.

^{102.} See SPS Agreement, supra note 40, art. 5, \P 5.

The Appellate Body decided this was not a closed list by adding its own language: "The risk . . . under Article 5.5 is not only risk ascertainable in a science laboratory . . . but also risk in human societies as they actually exist, in other words, the ætual potential for adverse effects on human health in the real world where people live and work and die." This suggests a scenario in which a party can include cultural preferences and social values in its risk assessment. Thus, the precautionary principle rejected by the panel, is revived in the Appellate Body decision, albeit in circumscribed form.

3. The Arbitration Decision Allowed the U.S. to Impose Countermeasures

The EU claimed that the Appellate Body ruling allowed it to carry out a new risk assessment while keeping the ban in place. The U.S. disagreed, arguing that the ban should now be lifted within the "reasonable amount of time" stipulated by Article 21, paragraph 3 of the DSU. Since neither party could agree on the timing, the matter was submitted to binding WTO arbitration under paragraph 3(c). The arbitrator ordered EU compliance within fifteen months, or by May 13, 1999. In accordance with the U.S. argument, the ruling stipulated that the EU could not hold off legislative change pending a new scientific assessment. 107

Fifteen months later, the EU had made no attempt to lift the ban, nor had it come up with a new risk assessment. The WTO approved a U.S. request for countermeasures and appointed an arbitration panel to determine the amount. In July 1999, the panel approved 100% ad valorem duties on a list of goods drawn up by the USTR¹⁰⁸ that could be imposed up to an amount of \$116.8 million.¹⁰⁹ The U.S. immediately imposed the

^{103.} See WTO Appellate Body Report, supra note 8, ¶ 187.

^{104.} See Rountree, supra note 11, at 628.

^{105.} *Id.* at 628–29.

^{106.} WTO Arbitrator Award, *supra* note 9, ¶ 48.

^{107.} See id.

^{108.} See WTO Arbitrators Decision, supra note 11, $\P\P$ 55, 84.

^{109.} Estimates of the damage to the U.S. cattle industry have ranged from \$100–500 million. *See* Rountree, *supra* note 11, at 610.

duties on selected goods from its list.¹¹⁰ Although the EU had shown willingness to negotiate before the arbitration decision, it later retreated.¹¹¹ This suggests that from the EU point of view, the amount was set too low for Coasean bargaining,¹¹² or, perhaps, that the socio-political payoff from non-compliance exceeded the harm from the tariffs.

Foreshadowing the protests in Seattle later that same year, local Parisians reacted to the imposition duties by pelting a McDonald's restaurant with apples, and the French town that produces Roquefort cheese placed a 100% per unit tax on Coca-Cola sold in local vending machines. In late November and early December 1999, highly publicized protestors turned an aborted WTO ministerial meeting into the "Battle in Seattle." A loose coalition of environmentalists, trade union members and others accused the WTO, among other things, of denying Europeans the right to eat hormone-free beef. It was a nadir in U.S. trade relations, a view President Clinton conceded to the distress of some observers, when he agreed with some of the protestors' complaints.

III. FORCING COMPLIANCE THROUGH TRADE SANCTIONS

A. WTO Countermeasures

The DSU encourages prompt compliance with recommendations and rulings of the Dispute Settlement Body ("DSB").¹¹⁷ Under Articles 21 and 22, however, the DSU contemplates three levels of response to non-compliance with a DSB decision.

^{110.} See WTO Arbitrators Decision, supra note 11, at Annex II. The list included onions, Roquefort cheese, goose liver, fruit juice, mustard and pork products.

^{111.} See Rountree, supra note 11, at 633.

^{112.} See id. (suggesting the EU lacked incentive to deal).

^{113.} See Anne Swardson, Something's Rotten In Roquefort: A New U.S. Tariff, Wash. Post, Aug. 21, 1999, at A1.

^{114.} See, e.g., David Postman et al., Clashes, Protests Wrack WTO; Police Use Tear Gas Against Blockade, Seattle Times, Nov. 30, 1999, at A1; John Burgess & Steven Pearlstein, Protests Delay WTO Opening, WASH. Post, Dec. 1, 1999, at A1.

^{115.} See Jodie T. Allen & Dori Jones Yang, Trade's Battle Hits Seattle, U.S. NEWS & WORLD REP., Dec. 13, 1999, at 20, 20.

^{116.} See id.

^{117.} DSU, supra note 5, art. 21, ¶ 1. The DSB was established under Article 2 of the DSU. Id. art. 2.

Under Article 21, paragraph 3, the DSU allows that if an immediate implementation of the DSB recommendation is "impracticable," the non-compliant country may have a "reasonable period of time" in which to comply.¹¹⁸ A reasonable period can be proposed by the non-compliant party if approved by the DSB.¹¹⁹ If the DSB does not approve, the time may be mutually agreed-upon by both parties.¹²⁰ If this too fails, the period of time will be determined by binding arbitration within ninety days of the adoption of the DSB ruling,¹²¹ as was the case in the beef hormone case. Article 21, paragraph 3(c) suggests that the arbitrator not exceed a period of fifteen months, although it allows discretion for a shorter or longer period.

The second level of response is for the parties to negotiation a "mutually acceptable compensation." Compensation is not monetary, but involves the lifting of trade barriers by the losing party, thereby supporting free trade principles. 123 Compensation is offered not only to the prevailing party, but to all WTO members.¹²⁴ It is, however, rarely used. By contrast, the third level of response, is purely bilateral in nature. It allows the prevailing country to suspend "concessions or other obligations under the covered agreements" to the noncompliant country.¹²⁵ Article 22, paragraph 3 lists the principles and procedures that determine approval of the proposed concessions that are to be suspended.¹²⁶ In general, the DSU requires, where possible, that suspended concessions affect the same sector(s) as those implicated in the DSB decision, or, failing that, sector(s) covered by the same trade agreement 127 It also requires that the level of suspensions are

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118. Id. art. 21, ¶ 3.
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^{119.} $Id. \ \P \ 3(a)$.

^{120.} Id. ¶ 3(b).

^{121.} *Id*. ¶ 3(c).

^{122.} DSU, *supra* note 5, art. 22, $\P\P$ 1-2.

^{123.} See Joost Pauwelyn, Enforcement and Countermeasures in the WTO: Rules are Rules-Toward a More Collective Approach, 94 Am. J. Int'l L. 335, 337 (2000).

^{124.} See, e.g., Japan—Taxes on Alcoholic Beverages, Mutually Acceptable Solution on Modalities for Implementation, WT/DS10/19, Doc. No. 98-0138 (Jan. 12, 1998), at http://www.wto.org/english/tratop_e/dispu_e/distabase_wto_members3_e.htm (Japan offered compensation in the form of tariff concessions for its delay).

^{125.} DSU, supra note 5, art. 22, $\P\P$ 1-3.

^{126.} *Id*.

^{127.} *Id.* ¶ 3(a)-(b).

quires that the level of suspensions are equivalent to the level of "nullification or impairment" found by the DSB.¹²⁸ If the non-compliant country objects to the level of suspensions proposed, or claims that the principles and procedures of Article 22, paragraph 3 were not followed, the country can refer the matter to arbitration, during which time concessions may not be suspended.¹²⁹

Although the Uruguay Round improved GATT rules for settling disputes, the DSU countermeasures reflect the GATT scheme of privately negotiated, bilateral treaties in contrast to the obligations of public international law. If a non-compliant country does not agree to comply, the WTO cannot force compliance. Instead, the prevailing country urges compliance by restricting its trade concessions.¹³⁰ In addition, unlike public international law, the DSU offers no remedy of reparation. There is only prospective relief, and this relief may be delayed by the reasonable period of time allowance and by arbitration.¹³¹ The bilateral nature of the suspension of concessions can disfavor prevailing countries who are politically or economically weaker than the non-compliant member. A small country may not want to suspend concessions against a larger country that may have greater economic impact on the withholding country, but may nevertheless affect the larger country's political decisions, such as granting aid. Less obviously, a large, politically powerful party such as the U.S. confronts a similar dilemma when enticing compliance through trade restrictions, as WTO rules lack binding authority.

The power to authorize countermeasures has been widely perceived as a way of giving backbone to a previously milquetoast GATT dispute settlement process. The threshold problem with this remedy is an inherent ideological contradiction that arises when an organization founded on the principle of free trade employs a measure that restricts trade. If this

^{128.} *Id*. ¶ 4.

^{129.} See Id. ¶¶ 6-7.

^{130.} *Id.* art. 3, \P 7. *See also* DSU, *supra* note 5, art. 22, \P \P 2-3.

^{131.} See DSU, supra note 5, art. 21, ¶ 3.

^{132.} See, e.g., Carolyn B. Gleason & Pamela D. Walther, The WTO Dispute Settlement Implementation Procedures: A System in Need of Reform, 31 LAW & Pol'y Int'l Bus. 709, 709 (2000).

^{133.} But see Daniel R. Murray, Foie Gras?: Making Economic Sense of the 1999 U.S. Tariffs on Gourmet European Goods, 5 J. Int'l Legal Stud. 243,

objection is waived, the effectiveness of sanctions can derive from their power to bring parties to the bargaining table. The threatened sanctions should, therefore, present a credible threat. In coming in at the low end of the harm, the WTO arbitration decision against the EU in the Beef Hormone dispute achieved the opposite result. It appears the EU has decided that the cost of non-compliance is affordable. Its political and cultural differences with the U.S. on this matter, and perhaps most importantly, the protection of its own beef industry, appears to be worth the punishment of export taxes. In this way, the tariffs do little to remedy the initial harm complained of by the U.S., while causing further harms to small American businesses as well as their European counterparts through import duties. Furthermore, the problem with countermeasures that are set too low to induce compliance is that they call into guestion the effectiveness of the dispute settlement processes. Countermeasures that were intended to be temporary¹³⁴ continue from year to year, and attention shifts to the failure of the settlement process to enforce compliance, rather than the lack of compliance itself.

Sanctions are a double-edged sword that hurt a large importing country, such as the U.S., as well as the exporting country they are intended to punish. This applies tenfold when the countries have the interdependent trading relationship like the one existing between the EU and U.S.¹³⁵ A glance at the products on the U.S. tariff list approved by WTO arbitrators in the Beef Hormone case reveals a tendency toward high-end food imports that presumably are calculated to strike a balance of minimum harm to the U.S. and maximum harm to the EU.¹³⁶ The process, however, does not rule out short-term casualties. The long-term harm is less tangible, but it clearly runs counter to U.S. goals of global free trade.

^{256 (1999) (}arguing that the tariffs are not protectionists but simply equivalent to the amount the U.S. has paid to subsidize EU beef producers).

^{134. &}quot;The suspension of concessions or other obligations are temporary measures available in the event that the recommendations and rulings are not implemented within a reasonable period of time." DSU, *supra* note 5, art. 22. ¶ 1.

^{135.} See generally NATO REPORT, supra note 12, at tbls.

^{136.} See Murray, supra note 133, at 252.

B. Section 301 Sanctions

Since 1974, the principal means of addressing allegedly discriminatory trade practices by foreign governments that adversely affect U.S. trade has been sections 301-310 of the Trade Act of 1974 (collectively "Section 301").¹³⁷ The provisions of the Act empower the President, through the USTR (an executive appointee)¹³⁸ to retaliate unilaterally with trade sanctions against any unjustifiable or discriminatory act or policy of a foreign country.¹³⁹

Although some trading partners thought that Section 301 would be replaced by the DSU, U.S. officials have stated with intricate reasoning that Section 301 measures may actually be more effective with the DSU.¹⁴⁰ In 1998, the U.S. invoked Section 301 against the EU in the EU-bananas dispute ("Bananas")¹⁴¹ in which the EU also had an adverse WTO ruling, and the U.S. contemplated countermeasures pursuant to Arti-

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^{137.} Trade Act of 1974 §§ 301-310, 19 U.S.C. §§ 2411-20 (2000).

^{138.} See Jay L. Eizenstat, Comment, The Impact of the World Trade Organization on Unilateral United States Trade Sanctions Under Section 301 of the Trade Act of 1974: A Case Study of the Japanese Auto Dispute and the Fuji-Kodak Dispute, 11 Emory Int'l L. Rev. 137, 139-40 (1997) (arguing that although Article II of the U.S. Constitution gives Congress the power to "regulate Commerce with foreign nations," that body has delegated authority to the executive branch in order to project a pro-sovereignty position in trade negotiations).

^{139.} See 19 U.S.C. § 2411(a)-(b)(1).

^{140.} See, e.g., Overview of the Results of the Uruguay Round: Hearing Before the Senate Committee on Commerce, Science, and Transportation, 103rd Cong. 12 (1994) (statement of Hon. Michael Kantor, U.S. Trade Representative); Results of Uruguay Round Trade Negotiations: Hearings Before the Senate Committee on Finance, 103rd Cong. 195 (1994) (statement of John H. Jackson, Hessel E. Yntema Prof. of Law, The University of Michigan Law School).

^{141.} This U.S.-EU case concerned the preferential treatment the EU gives banana imports from certain countries. See generally European Community – Regime for the Importation, Sale and Distribution of Bananas, Complaint by the United States, Report of the Panel, WT/DS27/R/USA, Doc. No. 97-2070 (May 22, 1997), at http://www.wto.org/english/tratop_e/dispu_e/distabase_wto_members2_e.htm [hereinafter EC-Bananas Panel Report]. The nine-year-old Bananas dispute was resolved by the Bush administration on Apr. 11, 2001. See Press Release, Office of the United States Trade Representative, U.S. Government and European Commission Reach Agreement to Resolve Long-Standing Banana Dispute (Apr. 11, 2001), available at http://www.useu.be/issues/bana0411.htm.

cle 22 of the DSU.¹⁴² The EU protested the use of Section 301 as an instance of unilateral enforcement by the U.S. inconsistent with its Article 23 obligations that endorsed multilateral enforcement of WTO decisions through the DSU.¹⁴³ The EU instigated a separate legal inquiry into the legitimacy of Section 301 within the dispute settlement process.¹⁴⁴ With great diplomacy, the WTO panel determined that despite the discretionary elements of the statute in sections 304, 305, and 306 that appeared to generate a prima facie inconsistency, the U.S. had pledged both before the WTO panel and in a Statement of Administrative Actions that it would not exercise this discretion contrary to its Article 23 obligations, and therefore exercising Section 301 sanctions were permissible.¹⁴⁵

Historically, the U.S. has used sanctions to open up otherwise inaccessible markets. It has been an effective tool that is popular with Congress. Since 1974, over ninety-eight cases have been filed under Section 301. According to one study, the threat of sanctions led to trade liberalization in 70% of cases, indicating that the successful use of sanctions can be attributed largely to the credible threat of retaliation and not in actually levying them. The clear implication for the Beef Hormone arbitration is that the WTO did not furnish the U.S. with an award that presented a credible threat.

^{142.} See EC-Bananas Panel Report, supra note 141, ¶ II.21.

^{143.} See Seung Wha Chang, Taming Unilateralism Under the Multilateral Trading System: Unfinished Job in the WTO Panel Ruling on U.S. Sections 301-310 of the Trade Act of 1974, 31 LAW & POL'Y INT'L BUS. 1151, 1155 (2000).

^{144.} See id.

^{145.} See id. See also United States – Sections 301-310 of the Trade Act of 1974, Report of the Panel, WT/DS152/R, Doc. No. 99-5454 (Dec. 22, 1999), at http://www.wto.org/english/tratop_e/dispu_e/distabase_wto_members4_e.htm.

^{146.} See Chang, supra note 143, at 1157.

^{147.} See Eizenstat, supra note 138, at 159.

^{148.} John H. Jackson, The World Trading System: Law and Policy of International Economic Relations 117 (1989). See also Thomas O. Bayard, Comment on Alan Sykes' "Mandatory Retaliation for Breach of Trade Agreements: Some Thoughts on the Strategic Design of Section 301," 8 B.U. Int'l L.J. 325, 325 (1990).

^{149.} See id.

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C. Carousel Retaliation

In May 2000, the first major trade legislation to pass Congress since 1995, the Africa-Caribbean Basin Initiative Bill ("Africa-CBI Bill") was signed into law by President Clinton. This bill contained provisions that allowed the USTR to employ a carousel approach to trade sanctions by rotating the products on its Section 301 list every six months. House Committee on Agriculture Chairman Larry Combest, a co-sponsor of the "Carousel Retaliation Act," described the economic impact of the provisions as "what comes around, goes around. Carousel sanctions attempt to give teeth to WTO countermeasures by testing the legal limits under Article 22 of the DSU. They do not challenge the bilateral nature of enforcement, nor the prospective nature of the remedy. 153

The WTO arbitration decision in the Beef Hormone dispute refers directly to carousel sanctions.¹⁵⁴ The report cites a U.S. promise: "Although nothing in the DSU prevents future changes to the list . . . the United States has no current intent to make such changes." It continues:

We thus assume that the U.S. – in good faith and based upon this unilateral promise – will not implement the suspension of concessions in a carousel manner. We therefore do not need to consider whether such an approach would require an adjustment in the way in which the effect of an authorized suspension is calculated. 156

^{150.} See Trade and Development Act of 2000, Pub. L. No. 106-200, 114 Stat. 251.

^{151.} See International Center for Trade and Sustainable Development, Africa-CBI Trade Bill Passes Senate; Carousel Provisions Ignite EU-US Tensions, at http://www.ictsd.org/html/weekly/story1.16-05-00.htm (last visited Feb. 24, 2002).

^{152.} Press Release, United States House of Representatives Committee on Agriculture, Combest, Stenholm Pursue New Strategy on Trade Violations Carousel Retaliation Act: What Comes Around Goes Around (Oct. 1, 1999), available at http://agriculture.house.gov/106/pr991001.html. See also H.R. 2991, 106th Cong. (1999).

^{153.} See Trade and Development Act of 2000, Pub. L. No. 106-200, 114 Stat. 251.

^{154.} See WTO Arbitrators Decision, supra note 11, ¶ 22.

^{155.} Id.

^{156.} Id.

Following passage of the Africa-CBI Bill, the EU requested DSU consultations with the U.S. alleging that the sanctions were impermissible:

Section 306, as amended, is in breach of the DSU since it mandates unilateral action without any prior multilateral control. . . . [The EU] further is of the view that the measure is in breach of the obligation of equivalence, in that it creates a structural imbalance between the cumulative level of the suspension of concessions and the level of nullification and impairment as determined under relevant DSU procedures.¹⁵⁷

The DSU allows sixty days for resolution of disputes through consultation; after that the EU could request a panel to rule on the complaint.¹⁵⁸ To date, the EU has not done this.

As a legal matter, carousel sanctions are not expressly outlawed by the DSU. A recent proposal by the Philippines and Thailand to amend Article 22, paragraph 7 of the DSU in a way that would make it harder to impose carousel sanctions, ¹⁵⁹ suggests that the DSU as it stands does not prohibit them. Furthermore, the short time-frame approach of carousel sanctions is supported by a DSU policy that stresses the temporary nature of countermeasures. ¹⁶⁰ The EU alleges that carousel sanctions violate the principle of equivalence under Article 22. ¹⁶¹ Paragraph 4 of Article 22 specifically states that "[t]he level of the suspension of concessions or other obligations authorized by the DSB shall be equivalent to the level of nullification or impairment." ¹⁶² In Article 22, paragraph 7, the DSU instructs that the arbitrator shall determine equivalence. ¹⁶³ Since the

^{157.} Pruzin, supra note 31.

^{158.} *Id*.

^{159.} See Daniel Pruzin, WTO: WTO Members Gear Up for Talks on Dispute Settlement Rules Reform, Int'l Trade Daily (BNA) (Oct. 11, 2001), at WL 10/11/2001 BTD d8.

^{160.} See DSU, supra note 5, art. 22, \P 8. "Prompt compliance with recommendations or rulings of the DSB is essential in order to ensure effective resolution of disputes to the benefit of all Members." *Id.* art. 21, \P 1.

^{161.} See S.K. Ross & Assoc., P.C., Good Trade – New Law Encourages African and Caribbean Commerce, at http://www.skralaw.com/Articles/trade_remedies.htm (last visited Feb. 24, 2002).

^{162.} DSU, supra note 5, art. 22, \P 4.

^{163. &}quot;The arbitrator acting pursuant to paragraph 6 [procedure for arbitration] shall not examine the nature of the concessions or other obligations to

approved tariffs can be interchanged on a pecuniary level so long as the total does not exceed the amount of nullification and impairment specified by the arbitrator, carousel sanctions do not violate pecuniary equivalence. According to the EU, however, the rotated products create an additional cumulative harm that exceeds equivalence. Unfortunately, it is not clear from the available record, how the EU quantifies this cumulative effect.

During consultations with the EU concerning carousel sanctions, the U.S. refused to disclose details of its carousel selection procedures. While this inscrutability may protect the process from a finding of illegality on the part of the EU, it is ironic coming from a party who has urged that the WTO processes become more transparent. In addition, although U.S. secrecy preserves its right to act unilaterally from multilateral interference, this posture raises questions of sovereignty that generally arise when power is ceded to a multilateral institution, rather than an executive appointee. Here, the USTR is appointed without a direct democratic mandate, and with questionable constitutional authority, is given a large amount of discretion to make decisions that adversely affect U.S. businesses.

be suspended but shall determine whether the level of such suspension is equivalent to the level of nullification or impairment." Id. ¶ 7.

- 164. See EU Request for Consultations, supra note 26.
- 165. See Telephone Interview, supra note 28. The U.S. stated that "carousel sanctions would be applied on a case by case basis, so no generalizations regarding their implementation could be made." Id. The U.S. position makes it "harder for the EU to build a WTO case against the carousel sanctions law." Id.
- 166. See Pruzin, supra note 159.
- 167. For further discussion of multilateralism versus sovereignty, see Julian G. Ku, *The Delegation of Federal Power to International Organizations: New Problems with Old Solutions*, 85 Minn. L. Rev. 71 (2000).
- 168. See, e.g., Eizenstat, supra note 138, at 139, 139 nn.11-12.
- 169. A limited amount of feedback concerning the targeted products is permitted. See, e.g., Implementation of WTO Recommendations Concerning the European Communities' Regime for the Importation, Sale and Distribution of Bananas, 64 Fed. Reg. 19209, 19210 (Office of the U.S. Trade Rep. Apr. 19, 1999) ("The articles affected by this determination [Section 301 sanctions] were selected in light of the comments submitted to the Section 301 Committee in response to the October 22, November 10, and December 23 notices, and the testimony presented at the public hearing held on December 9, 1998.").

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According to a USTR official, the same methods used to select Section 301 products are used to choose the businesses targeted for carousel sanctions.¹⁷⁰ First, a broad list is compiled by government analysts for the Department of Commerce and USDA, who comb through the tariff rates for every listed product and its accompanying trade statistics.¹⁷¹ Analysts look for rates that are proportional, and in cases where reciprocal products can be found, they are targeted.¹⁷² For instance, in the Beef Hormone case, the U.S. initially targeted pork products.¹⁷³ The overriding goal is to pick those products where duties will hurt the other side more than the U.S., but this process is more art than science.¹⁷⁴ When dealing with the EU, which Member State to target also becomes part of the selection equation.¹⁷⁵ Thus, after selecting pork products, the U.S. scaled back the quantity of products targeted because it did not want to unfairly burden Denmark, the EU's largest pork producer, as Denmark is a relatively small EU Member State lacking large political influence.¹⁷⁶ After compilation, the broad list is then published and disseminated throughout government and industry to give notice and solicit comment.¹⁷⁷ Responses to carousel sanctions from industries targeted by Section 301 have been predictable: those already on the list like them because it means they will rotate off more quickly, those off the current list dislike them because they are now at risk of selection in the next time period.¹⁷⁸

If carousel sanctions are found to be legal, their use by the U.S. in the time-worn Beef Hormone dispute is perhaps irresistible. The arbitration award has had little observable effect on the EU, whereas the mere threat of carousel sanctions has already caused the EU to jump.¹⁷⁹ Beyond the general problems with sanctions – they work better as threats, and when used cut both ways – are those particular to a rotating list of

^{170.} See Telephone Interview, supra note 28.

^{171.} See id.

^{172.} See id.

^{173.} See id.

^{174.} See id.

^{175.} See id.

^{176.} See Telephone Interview, supra note 28.

^{177.} See id.

^{178.} See id.

^{179.} See, e.g., EU Request for Consultations, supra note 26.

businesses. The first problem is the shadowy product selection process with few procedural safeguards to ensure equity, and even fewer objective measures of substantive equity. A broader range of targets may increase equity by spreading the pain more thinly on the U.S. side while maintaining pressure on the EU, but unless the process is open to analysis, this cannot be studied. A second problem is the ill-will the sanctions will engender in the trans-Atlantic business community. The use of carousel sanctions is a political as well as legal decision, and it affects a widely dispersed range of small businesses on both sides of the Atlantic that may not be politically well organized.

IV. ALTERNATE WAYS OF ENFORCING COMPLIANCE

As flaws in the DSU process have become apparent, scholars and international trade experts have proposed solutions.¹⁸¹

A. Reforming the DSU

An obvious solution to questions raised by the Beef Hormone case is to look at the problems with the DSU and attempt repair by changing the process. 182 The most glaring fault is the time it takes to give an injured party relief. 183 Although it was a goal of the U.S. GATT negotiators to impose "stringent time limits on each step of the settlement process,"184 the length of time this case has taken despite favorable rulings at each step has brought the U.S. no closer to its desired goal, or indeed that of the DSU as expressed in Article 22, paragraph 1: "neither compensation nor the suspension of concessions or other obligations is preferred to full implementation of recommendation to bring a measure into conformity, with the covered agreements." In practice, temporary suspension has been too long in arriving and lasted too long in operation. The arbitrators in the Beef Hormone dispute interpreted the "reasonable period of time," articulated in Article 21, paragraph 3(c) during which the losing party brings its regulations into conformity, as

^{180.} See Yerkey, supra note 36.

^{181.} See, e.g., Gleason & Walther, supra note 132, at 728-35.

^{182.} See id. at 734.

^{183.} See id. at 713.

^{184.} SAA, *supra* note 22.

^{185.} DSU, supra note 5, art. 22, ¶ 1.

"the shortest period possible within the legal system of the Member to implement the recommendations and rulings of the [Dispute Settlement Body]." The EU procedures, however, dictated the full fifteen month grace period. Abuse of time by the losing party is not contemplated by the DSU.

A non-compliant party has few obligations during the grace period. Under Article 21, it must provide regular status reports beginning six months after the period begins, but nothing prevents a losing party from using the period to buy additional months of non-compliance. Additional monitoring and surveillance during this period could prevent bad faith simply by its presence or by tolling the time period in the face of abuse.

Incentives under the current regime are also minimal. Since suspension of concessions is not granted retrospectively, the losing country has no reason to speed up implementation even if good faith is assumed. Commentators have suggested that requiring compliance, compensation, or withdrawal of concessions at the time of the WTO ruling would be more effective, and has been shown to work in the North American Free Trade Agreement. Alternatively, along with greater surveillance during the grace period, imposition of double and treble damages would discourage bad faith during the implementation period. Others have suggested that the WTO should be permitted to levy retrospective reparations similar to those awarded by the International Court of Justice. 191

B. Other Ideas

1. Compensating Trade Liberalization Measures

In November 2000, a CEO-level conference of the Trans-Atlantic Business Dialogue suggested that in place of sanctions, the U.S. and EU should look to "compensating trade lib-

^{186.} WTO Arbitrator Award, *supra* note 9, ¶ 26.

^{187.} Id. ¶ 48.

^{188.} See, e.g., Gleason & Walther, supra note 132, at 720-21 (describing strong evidence of non-compliance well before expiration of the reasonable period in the Bananas case).

^{189.} See id. at 733-34.

^{190.} See id. at 734-35.

^{191.} See Pauwelyn, supra note 123, at 339.

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eralization measures."¹⁹² This asks the non-compliant country to lower its tariffs on other goods in such a way as to offset the WTO violation.¹⁹³ This proposal takes even more control away from the injured party, but has the virtue of promoting free trade.

2. Multilateralism

One noted scholar has commented on the DSU (specifically, Articles 3 paragraph 4; 3 paragraph 5; 3 paragraph 7; 11; 19 paragraph 1; 21 paragraph 1; 21 paragraph 6; 22 paragraph 1; 22 paragraph 2; 22 paragraph 8; and 26 paragraph 1(b)) by suggesting that the "overall gist" of the provisions "strongly suggests that the legal effect of an adopted panel report is the international law obligation to perform the recommendation of the panel report." 194 Although this is an extreme position to take at this time, and few countries would likely accept an international obligation based on an overall gist, it can be interpreted as a forward-looking statement, signaling the path the WTO is slowly taking toward multilateralism. Support for reading WTO rules and DSU decisions as binding international obligations has been found in DSU Article 3 paragraph 2 that provides that WTO provisions are clarified "in accordance with customary interpretations of public international law."195 Multilateral treaties, such as the SPS Agreement, which are no longer based on the traditional balance of trade concessions between parties, indicate that the WTO is venturing beyond the original bilateral GATT framework. 196 Under this analysis, enforcement of WTO obligations will become a multilateral rather than a bilateral concern. In summary:

Once WTO rules have been accepted as international legal obligations that affect individuals and merit collective en-

^{192.} Transatlantic Business Dialogue, Cincinnati Recommendations 37 (2000), available at http://www.tabd.com/recommendations/Cincinnati00.pdf (last visited Feb. 24, 2002).

^{193.} See Yerkey, supra note 36.

^{194.} John H. Jackson, *The WTO Dispute Settlement: Understanding Misunderstandings on the Nature of Legal Obligation*, 91 Am. J. Int'l L. 60, 62-63 (1997).

^{195.} Pauwelyn, supra note 123, at 341.

^{196.} The customary rationale for enforcement of these agreements has become "less relevant." *Id.* at 342.

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forcement for the public good . . . and once this new perception has come to be accepted and entrenched, it will be increasingly difficult to justify both the absence of certain traditional remedies, including reparation, and the lack of a more effective system to induce compliance with WTO rules. ¹⁹⁷

V. Conclusion

The political and cultural differences between the EU and U.S. that have been highlighted by the Beef Hormone dispute relate to differing attitudes toward food and science. They were exacerbated by health crises in EU Member States and the economic and political pressures of multi-million dollar agribusiness. The acceptance of genetically modified organisms is running into similar problems in Europe, and may ultimately raise more complex issues for the WTO. 198 The failures of the DSU and SPS Agreement with regard to the Beef Hormone case may ultimately prove fruitful for future amendments to the procedure.

In the meantime, the American beef industry is suffering, and the U.S. has nothing to show after fifteen years of friction with its largest trading partner and many favorable WTO rulings. With regard to this dispute, the use of carousel sanctions, if they are indeed legal, may seem justified by the length of time the dispute has run, the bad faith evidenced by the EU's lack of compliance and the economic equality between these two giant trading partners. It is clear that DSU procedures alone have failed both to enforce timely and appropriate counterme asures on a non-compliant party, and to ensure that the countermeasures are a temporary predecessor to compliance. As suggested, it may be that multilateral treaties such as the SPS Agreement at issue in the Beef Hormone dispute may herald a future where multilateral legal obligations replace bilateral trade sanctions, and prove more effective in policing compliance with WTO rulings. All present indications suggest, however, that progress along these lines will be slow and politically volatile. 199 In reality, trade talks take place in a political climate and in the context of many different disputes and is-

^{197.} Id. at 347.

^{198.} See, e.g., Echols, supra note 13, at 528-29, 538 (describing the EU's demand that foods containing genetically modified organisms be labeled).

^{199.} See supra notes 114-16 and accompanying text.

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sues.²⁰⁰ Thus, other considerations altogether may influence the ultimate settlement of the Beef Hormone dispute without regard to its extensively litigated merits.

200. Currently, for example, the EU has asked the WTO to consider countermeasures of \$4 billion against the U.S. as a result of its favorable tax treatment to foreign sales corporations, while in early March 2002, the U.S. announced tariffs on imported steel that have alarmed affected WTO member countries. $See\ Pruzin,\ supra\ note\ 30.$

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LEGAL STRATEGIES FOR CHALLENGING THE CURRENT EU ANTI-DUMPING CAMPAIGN AGAINST IMPORTS FROM CHINA: A CHINESE PERSPECTIVE

Hongliu Gong*

I. INTRODUCTION

Over the past twenty years, trade relations between the European Union ("EU") and China have been growing dramatically. Consider the imports into the EU from China. The value increased thirty-fold, from 2.107 billion euros in 1980, to 70.103 billion euros in 2000, covering a variety of products like machinery, chemical products textiles and clothing.¹ Today, China is the EU's third most important trading partner (after the United States and Japan), and the EU continuously maintained a trade deficit with China in the amount of roughly 32 billion euros during the first nine months of 2000.²

This may partly explain why there has been an accelerated anti-dumping campaign in recent years within the EU against Chinese products.³ Chinese industries, whose competitiveness has increased in the European market, inevitably upset their European counterparts. It has further triggered the EU's anti-

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^{1.} Europa, *Bilateral Trade Relations: China, Statistics, at* http://europa.eu.int/comm/trade/pdf/bilstat/econo_china.xls (last visited Feb. 24, 2002) [hereinafter Europa I].

^{2.} Id. See also Europa, Overview: Bilateral Trade and Investment Relations, at http://europa.eu.int/comm/trade/bilateral/china/china.htm (last visited Feb. 24, 2002).

^{3.} See Ke Ma, Women Wei Shenmo Zong Bei Fan Qingxiao? [Why Have We Always Been Targeted by the Anti-Dumping Campaigns?], SOUTHERN WEEKLY (Aug. 18, 2000) (on file with Journal).

dumping process, where European companies continue to initiate anti-dumping proceedings to defend their own regimes. But a more important reason relates to China's "quasi-market economy" status under EU anti-dumping law and practice.⁴ In most cases, the European Commission ("Commission") and the Council of the European Union ("Council") have regarded China as a non-market economy ("NME") country, and applied arguably discriminatory methodology and unfair policy in determining the margin of dumping and injury to alleged Chinese exporters/producers. Thus, an artificially high dumping/injury margin would easily be established.⁵

As a result, China has become one of the most significant targets in the EU anti-dumping practice. Since 1988, anti-dumping proceedings against China have substantially increased.⁶ Even worse from this perspective, most of the proceedings against Chinese enterprises resulted in high anti-dumping duties or minimum undertakings.⁷

By the end of 1999, the Commission and Council had 151 anti-dumping measures and five anti-subsidy measures in force, covering sixty-three products and thirty-five countries. Of these 156 measures, thirty-three concerned China, eleven concerned Russia and eleven measures applied to other NME countries. In other words, the EU anti-dumping measures against China accounted for 21% of the whole, and 35% of those concerned NME countries.⁸ These measures severely undermined the competitive capability of many Chinese industries involved, and virtually excluded them from the European market. In this sense, China has also become the most distinctive victim of the EU anti-dumping practice.⁹

^{4.} *Id*.

^{5.} See Donghui Fu, EC Anti-Dumping Law and Individual Treatment Policy in Cases Involving Imports from China, 31 J. WORLD TRADE 73, 78-79 (1997).

^{6.} *Id*.

^{7.} Overview of the Monitoring of Third Country Safeguard Cases and of the Implementation of the Trade Barriers Regulation: Eighteenth Annual Report from the Commission to the European Parliament on the Community's Anti-Dumping and Anti-Subsidy Activities, COM(00)440 final at 19-20, available at http://europa.eu.int/comm/trade/pdf/adrep_2000_en.pdf (last visited Feb. 12, 2002) [hereinafter Eighteenth Annual Report].

^{8.} *Id*.

^{9.} See Ma, supra note 3.

In this Article, from a Chinese perspective, the author will suggest legitimate and effective strategies for challenging the current EU anti-dumping campaign against imports from China. Part II will illustrate the EU anti-dumping law applicable to imports from China. Part III will discuss the EU anti-dumping practice in relation to China. Part IV will describe the impact of the campaign on Chinese industries and emphasize the necessity for a Chinese challenge. Part V will propose a series of legal strategies for China to achieve the goal of true fair trade. Part VI will draw a conclusion.

II. EU ANTI-DUMPING LAW APPLICABLE TO IMPORTS FROM CHINA

Dumping is a major aspect of the unfair trading practice in the EU's external trading relations.¹⁰ Determination of dumping depends on three elements: (1) normal value; (2) export price; and (3) dumping margin (a result of the comparison of the former two).¹¹ According to the EU anti-dumping legislation, "A product is to be considered as being dumped if its export price to the Community is less than a comparable price for the like product, in the ordinary course of trade, as established for the exporting country."¹² Here, the comparable price means the normal value at which exporters sell goods on their domestic market.¹³ In the EU anti-dumping practice, the targeted exporting countries are categorized as either a market economy ("ME") or an NME. The functioning of the EU anti-dumping instrument is based on these two respective categories.¹⁴

The main practical difference between the treatment of an ME and an NME is related to the methodologies adopted to determine the existence of dumping for the purpose of anti-

^{10.} Trade in Action, Trade Policy Instrument: On Guard for Unfair Practice (2001), available at http://europa.eu.int/comm/trade/policy/index_en.htm (last visited Feb. 24, 2002).

^{11.} Council Regulation 384/96 on Protection Against Dumped Imports from Countries Not Members of the European Community, art. 2, 1996 O.J. (L 56) 1, 4.

^{12.} Id. art. 1(2).

^{13.} See id. art. 2(1).

^{14.} Jianyu Wang, A Critique of the Application to China of the Non-Market Economy Rules of Antidumping Legislation and Practice of the European Union, 33 J. WORLD TRADE 117, 119-20 (1999).

dumping investigation.¹⁵ For the exporters from an ME country, normal value is based on their own domestic price. For those who come from NME countries, the calculation relies on an analogue country methodology, which means normal value is based on the domestic price of an analogue country selected, other than that of the exporter's own country.¹⁶ Adoption of the analogue country methodology seems merely a technical matter, but in fact is vital. It makes the dumping margin artificially high, and subsequently leads to a large amount of the anti-dumping duty imposed on exporters.¹⁷

Unless it is evident that a dumped product has caused the "material injury" to certain industries of the EU, no antidumping measure will be taken against this product.¹⁸ So, the evaluation of injury is a primary step for an anti-dumping proceeding. Another primary step is the consideration of community interests.¹⁹

In general, the legal sources of the EU anti-dumping instrument are at three levels. The primary source is the "common commercial policy" ("CCP") laid down in Article 133 (ex Art. 113) of the Treaty Establishing the European Community.²⁰ It provides that the CCP "shall be based on uniform principles, particularly in regard to . . . export policy and measures to protect trade such as those to be taken in the event of dumping or subsidies."²¹

Subject to the CCP, the Council has developed a comprehensive body of regulations to govern dumped imports from outside countries.²² These are secondary sources of EU anti-dumping law. Due to their operative and administrative nature, Council Regulations are the major source of law governing most aspects

^{15.} Id. at 120.

^{16.} See Council Regulation 384/96, supra note 11, art. 2(1).

^{17.} Fu, *supra* note 5, at 81.

^{18.} Council Regulation 384/96, supra note 11, art. 3.

^{19.} See id. art. 21.

^{20.} Treaty Establishing the European Community, Nov. 10, 1997, art. 113, O.J. (C 340) 3, 237 (1997), available at http://europa.eu.int/eurlex/en/treaties/dat/ec_cons_treaty_en.pdf (last visited Feb. 12, 2002).

^{21.} Id.

^{22.} See Eighteenth Annual Report, supra note 7, at 12. See generally Council Regulation 384/96, supra note 11; Council Regulation 2026/97, 1997 O.J. (L 288) 1.

of the EU anti-dumping practice, providing general principles and implementing rules.²³

Case law is the third major source of EU anti-dumping law.²⁴ With a competence to review anti-dumping cases, the European Court of Justice ("ECJ") and the European Court of the First Instance ("CFI") hear a large number of such cases to ensure correct implementation of EU rules. The judgments of these courts constitute another concrete legal basis for the EU anti-dumping instrument.²⁵

A. Brief Legislative History

The first anti-dumping law of the European Community ("EC") on "protection against dumping or the granting of bounties or subsidies by countries which are not members" was passed on April 5, 1968.²⁶ Since then, legislation in this field has developed over the last thirty years, reflecting the result of the General Agreement on Tariffs and Trade ("GATT") negotiations, judgments of the ECJ, new accessions to the EU or simple procedural or substantive refinements.²⁷ Of course, the changing economic situation of the EU's external trading partners, particularly NME countries, has also been taken into account.

The first law codifying the EC anti-dumping practice towards NME countries was Council Regulation 1681/79, introduced in 1979.²⁸ It contained a hierarchy of discriminatory special rules for calculating the normal value of products originating in NME countries.²⁹ Three years later, the EC promulgated Council Regulations 1765/82³⁰ and 1766/82,³¹ indirectly enu-

^{23.} See infra Part II.A. for an elaboration.

^{24.} See Eighteenth Annual Report, supra note 7, at 16, 90-93.

^{25.} Id.

^{26.} Council Regulation 459/68 on Protection Against Dumping or the Granting of Bounties or Subsidies by Countries Which are Not Members of the European Economic Community, art. 1, 1968 O.J. (L 93) 1, 2.

^{27.} See Wang, supra note 14, at 119.

^{28.} Council Regulation 1681/79 Amending Council Regulation 459/68 on Protection Against Dumping or the Granting of Bounties or Subsidies by Countries Which are Not Members of the European Economic Community, 1979 O.J. (L 196) 1.

^{29.} See id.

^{30.} Council Regulation 1765/82 on Common Rules for Imports from State-Trading Countries, 1982 O.J. (L 195) 1.

merating a number of NME countries to which the special antidumping rules should apply. China was counted as one of those countries.³² In 1994, the two Regulations were repealed and replaced by Council Regulation 519/94, of which Annex 1 listed a group of countries considered as "state-trading countries" for anti-dumping calculation purposes.³³ China subsequently was covered in that list.³⁴

The special anti-dumping rules applicable to NME countries continuously developed and were recently laid down in Article 2(7) of Council Regulation 384/96 ("Basic Anti-dumping Regulation" or "Basic Regulation") as the analogue country methodology.³⁵ Since its passage in 1995, the Basic Regulation has been the primary anti-dumping legislation of the EU.³⁶ Article 9(5) further codified a one country, one duty rule, and applied it to NME countries.³⁷

In April 1998, the EU issued a new regulation, Council Regulation 905/98 ("New Anti-dumping Rule"), to amend Article 2(7) of the Basic Regulation.³⁸ The amendment eliminated China from the list of NME countries, and replaced the analogue country methodology with a case-by-case approach.³⁹ In the case of China, it means that the domestic prices and costs of the targeted Chinese products may be used to calculate normal value in the anti-dumping proceedings against imports if the country met certain criteria.⁴⁰ Regulation 905/98 represented significant progress in EU legislation, as it reflected efforts and intent to make the anti-dumping instrument adherent to the

^{31.} Council Regulation 1766/82 on Common Rules for Imports from the People's Republic of China, 1982 O.J. (L 195) 21.

^{32.} See Wang, supra note 14, at 119.

^{33.} Council Regulation 519/94 on Common Rules for Imports from Certain Third Countries and Repealing Regulation 1765/82, 1766/82 and 3420/83, Annex 1, 1994 O.J. (L 67) 89, 97.

^{34.} See Wang, supra note 14, at 119.

^{35.} Council Regulation 384/96, supra note 11, art. 2(7).

^{36.} See Wang, supra note 14, at 119.

^{37.} See Council Regulation 384/96, supra note 11, art. 9(5).

^{38.} Council Regulation 905/98 Amending Council Regulation 384/96 on Protection against Dumped Imports from Countries Not Members of the European Community, art. 1, 1998 O.J. (L 128) 18, 19.

^{39.} Id. art. 1.

^{40.} See id.

changing economic reality of the EU's NME trading partners so as to act "appropriate[ly]." 41

B. Current Applicable Law

Today, having experienced many amendments and changes in practice, the EU anti-dumping law applicable to imports from China as well as other NME countries is moving along toward greater maturity. The analogue country methodology and the one country, one duty rule, which have long been the cornerstone of the EU anti-dumping instrument against NME trading partners, and have long been severely criticized by Chinese scholars and practitioners as "discriminatory" and "unfair," are phasing out as the EU introduces a new case-bycase approach into the anti-dumping practice against China and Russia. 43

Such progress has been fixed by two Council Regulations currently in force: The Basic Anti-dumping Regulation and the New Anti-dumping Rule. As the primary anti-dumping law, the Basic Regulation provides general principles, overall procedures and guidelines for most of the substantive issues within the EU.⁴⁴ The general principles cover: (1) definitions of dumping and dumping-related factors (such as normal value, and like products); (2) determinations of dumping, injury and EU industry; (3) consultation; (4) verification visits; (5) non-cooperation; (6) confidentiality; and (7) disclosure.⁴⁵ Despite frequent and sometimes significant alterations in anti-dumping legislation, these general principles have continued unchanged.

The Basic Regulation also establishes a set of procedures for the operation of each anti-dumping proceeding, regardless of which country the targeted imports come from, whether MEs or NMEs. The overall procedures are illustrated as: (1) initiation of proceedings; (2) investigation; (3) provisional measures; (4) undertakings; (5) termination without measures/imposition of definitive duties; and (6) duration, reviews and refunds. 46

^{41.} Id. at 18.

^{42.} Fu, *supra* note 5, at 79.

^{43.} See Council Regulation 905/98, supra note 38, art. 1.

^{44.} See Council Regulation 384/96, supra note 11.

^{45.} See id. art. 1.

^{46.} See id. arts. 5-9, 11.

Article 2(7) of the Basic Regulation sets forth the analogue country methodology applied to imports from enumerated NME countries (including China) for calculation of normal value. It provides:

In the case of imports from non-market economy countries . . . normal value shall be determined on the basis of the price or constructed value in a market economy third country, or where those are not possible, on any other reasonable basis, including the price actually paid or payable in the Community for the like product, duly adjusted if necessary to include a reasonable profit margin. An appropriate market economy third country shall be selected in a not unreasonable manner ⁴⁷

Article 9(5) of the Basic Regulation sets forth the one country, one duty rule applied to imports from enumerated NME countries in imposition of anti-dumping duty. It provides:

An anti-dumping duty shall be imposed in the appropriate amounts in each case, on a non-discriminatory basis The Regulation imposing the duty shall specify the duty for each supplier or, if that is impracticable, and as a general rule in the cases referred to in Article 2(7), the supplying country concerned. ⁴⁸

Accordingly, under the one country, one duty rule, the EU treats all suppliers of a certain industry from China as a unified body, therefore denying the individual export prices charged by each supplier, and imposing a single anti-dumping duty on all the suppliers concerned.⁴⁹ As the result of this rule, even an innocent Chinese exporter who does not commit dumping is subject to a duty, if other Chinese exporters in its industry do so. Further, the cooperating exporters have to pay a higher anti-dumping duty than their dumping margin, since a single duty rate is calculated on the basis of the average export prices of all the cooperating and non-cooperating exporters.⁵⁰ In addition, the export price of non-cooperating exporters is

^{47.} See id. art. 2(7).

^{48.} See id. art. 9(5).

^{49.} Fu, supra note 5, at 80.

^{50.} *Id*.

always determined on the basis of the facts then available, which can lead to a very high dumping margin.⁵¹

It is notable that the application of the one country, one duty rule in the EU anti-dumping practice against China is not exclusive, as some exceptions followed on occasion.⁵² Those exceptions are subject to an "individual treatment" policy, under which the individual export prices charged by each accused Chinese exporter/producer would be counted to calculate an individual dumping margin, and any anti-dumping duty that may be imposed would be a specific one based on the particular situation.⁵³

However, the implementation of the individual treatment policy by the EU is neither consistent nor predictable. In the 1990 "Tungsten Ores and Concentrate" case, the Commission determined separate dumping margins of 47.4% and 53.2% for two Chinese state trading companies, the China National Non-Ferrous Metals Import & Export Corporation and the China National Metals and Minerals Import & Export Corporation. ⁵⁴ Subsequently, separate provisional duties were set for, and undertakings were offered to the two companies. But the EU did not explicitly pronounce any rules in this case to explain on what grounds it granted individual treatment. ⁵⁵

It was in the 1991 matter of "small-screen colour television[s]" ("SCTVs") that the Commission and Council set up the relevant rules to examine whether individual treatment should

^{51.} *Id*.

^{52.} See id. at 81, 84.

^{53.} Id. at 81.

^{54.} Commission Regulation 761/90 Imposing a Provisional Anti-Dumping Duty on Imports of Tungsten Ores and Concentrates Originating in the People's Republic of China, and Terminating the Proceeding Concerning Imports Originating in Hong Kong, 1990 O.J. (L 83) 23, 24-25. See also Council Regulation 2735/90 Imposing a Definitive Anti-Dumping Duty on Imports of Tungsten Ores and Concentrates Originating in the People's Republic of China and Definitive Collecting the Provisional Anti-Dumping Duty, 1990 O.J. (L 264) 1; Commission Decision 478/90 Accepting Undertakings Offered by Certain Exporters in Connection with the Anti-Dumping Proceeding Concerning Imports of Tungsten Ores and Concentrates Originating in the People's Republic of China and Terminating the Investigation with Regard to these Exporters, 1990 O.J. (L 264) 55.

^{55.} See Fu, supra note 5, at 84.

be granted to Chinese exporters.⁵⁶ In this case, individual treatment was granted to Chinese joint-ventures with foreign investment, but not to state-owned companies.⁵⁷ Rules in the SCTVs matter were confirmed in other cases, for example "video tapes" in 1991,⁵⁸ and "certain polyester yarns" in 1992.⁵⁹ However, in the 1993 "bicycles" matter, the EU changed the policy, and individual treatment for Chinese companies was systematically refused.⁶⁰

In April 1998, the New Anti-dumping Rule replaced Article 2(7) of the Basic Regulation and introduced a new case-by-case approach to the EU anti-dumping practice against China and Russia.⁶¹ The New Anti-dumping Rule is composed of three subparagraphs. Subparagraph (a) maintains the provision of the original Article 2(7) of the Basic Regulation.⁶² Subparagraph (b) inserts the new case-by-case approach. It provides:

- 56. See Commission Regulation 129/91 Imposing a Provisional Anti-Dumping Duty on Imports of Small-Screen Colour Television Receivers Originating in Hong Kong and the People's Republic of China, 1991 O.J. (L 14) 31; Council Regulation 2093/91 on Imposing a Definitive Anti-Dumping Duty on Imports of Small-Screen Colour Television Receivers Originating in Hong Kong and the People's Republic of China and Collecting Definitively the Provisional Duty, 1991 O.J. (L 195) 1.
 - 57. See Council Regulation 2093/91, supra note 56, at 5.
- 58. Commission Regulation 1034/91 Imposing a Provisional Anti-Dumping Duty on Imports of Video Tapes in Cassettes Originating in the People's Republic of China, 1991 O.J. (L 106) 15; Council Regulation 3091/91 Imposing a Definitive Anti-Dumping Duty on Imports of Video Tapes in Cassettes Originating in the People's Republic of China and Definitively Collecting the Provisional Duty, 1991 O.J. (L 293) 2.
- 59. Commission Regulation 2904/91 Imposing a Provisional Anti-Dumping Duty on Imports of Certain Polyester Yarns (Man-Made Staple Fibres) Originating in Taiwan, Indonesia, India, the People's Republic of China and Turkey and Terminating the Anti-Dumping Proceeding in Respect of Imports of These Yarns Originating in the Republic of Korea, 1991 O.J. (L 276) 7; Council Regulation 830/92 Imposing a Definitive Anti-Dumping Duty on Imports of Certain Polyester Yarns (Man-Made Staple Fibres) Originating in Taiwan, Indonesia, India, the People's Republic of China and Turkey and Collecting Definitively the Provisional Duty, 1992 O.J. (L 88) 1.
- 60. Commission Regulation 550/93 Imposing a Provisional Anti-Dumping Duty on Imports of Bicycles Originating in the People's Republic of China, 1993 O.J. (L 58) 12, 18-19; Council Regulation 2474/93 on Imposing a Definitive Anti-Dumping Duty on Imports Into the Community of Bicycles Originating in the People's Republic of China and Collecting Definitively the Provisional Anti-Dumping Duty, 1993 O.J. (L 228) 1, 3-4.
 - 61. Council Regulation 905/98, supra note 38, art. 1.
 - 62. *Id*.

In anti-dumping investigations concerning imports from . . . the People's Republic of China, normal value will be determined in accordance with paragraph 1 to 6, if it is shown, on the basis of properly substantiated claims by one or more producers subjective to the investigation and in accordance with the criteria and procedures set out in subparagraph (c) that market economy conditions prevail for this producer or producers in respect of the manufacture and sale of the like product concerned. When this is not the case, the rules set out under subparagraph (a) shall apply. ⁶³

Accordingly, China is not automatically designated as an ME country, so the targeted Chinese industries will not be entitled to full ME status in the determination of normal value and export price, unless they can prove the existence of prevailing ME conditions listed in subparagraph (c).

Subparagraph (c) illustrates five cumulative criteria for granting ME status to the Chinese or Russian companies under investigation for dumping, and puts the burden of proof on these companies. These accused companies need to prove they meet the following:

- (1) Decisions of firms are taken without significant State interference and are made in response to market signals;
- (2) Accounts must be independently audited in line with international accounting standards;
- (3) Production costs and the financial situation of the company are not affected by distortions carried over from the former State-led economic system, barter trade or compensation of debts;
- (4) Companies are subject to bankruptcy and property law; and
- (5) Exchange rate conversations are carried out at market rates. ⁶⁴

With the New Anti-dumping Rule in force, Article 9(5) of the Basic Regulation is consequently altered. A more flexible case-by-case approach has replaced the one country, one duty rule.

^{63.} Id.

^{64.} Commission Proposal for a Council Regulation Amending Regulation 384/96 on Protection Against Dumped Imports from Countries Not Members of the European Community, COM(00)363 final at 6, available at http://europa.eu.int/eur-lex/en/com/pdf/2000/com2000_0363en01.pdf (last visited Feb. 24, 2002) [hereinafter Commission Proposal].

The accused Chinese exporters/producers will be assessed an individual anti-dumping duty other than a country-wide duty as long as they meet the criteria provided in the New Anti-dumping Rule.

III. EU ANTI-DUMPING PRACTICE IN RELATION TO CHINA

A. Historical Overview

Europe has been an export market for Chinese goods for many years. In the early years, the anti-dumping duty was employed to block Chinese light industrial products, including shoes, suitcases and bags from entering the European market. Later, the target shifted to mechanical and electronic products. 66

The first EU anti-dumping matter against China was its investigation of "saccharin," initiated in 1979.67 But the brunt of the campaign against China began in 1988 when China carried out its open policy and commenced national economic reform, which succeeded in bringing about an increase in China-EU trade interactions.68 Between 1990 and 1994, the EU initiated 166 anti-dumping investigations against imports from thirty-two non-Member States, among which twenty-five were against China, with thirty-one products (involving the chemical, electronic, and iron and steel sectors, and other light industries) subject to EU measures.69 Later, during the five-year period from 1995 to 1999, 218 investigations were initiated on imports from thirty-nine non-Member States.70 China was one of two main countries concerned, with twenty-nine investigations against her.71 The other was India, with twenty-five cases.72

^{65.} See Europa I, supra note 1.

^{66.} Boob Tube Ballyhoo: China TV Makers Unite to Challenge EU Anti-Dumping Charges, China Online (July 6, 2000), at http://www.chinaonline.com [hereinafter Boob Tube].

^{67.} Notice of Initiation of Anti-Dumping/Anti-Subsidy Procedure Concerning Saccharin and its Salts Originating in China, Japan and the USA, 1979 O.J. (C 207) 4.

^{68.} See Fu, supra note 5, at 73-74.

^{69.} Id. at 74-75.

^{70.} Eighteenth Annual Report, supra note 7, at 20.

^{71.} *Id.* at 127.

^{72.} Id.

A rapid growth of the EU anti-dumping campaign against China is reflected in the SCTVs matter.⁷³ Chinese color televisions first entered the European market in the 1980's. Currently, annual exports of Xiamen Overseas Chinese Electronic Co. Ltd. ("XOCECO") sets alone are between 400,000 and 500,000 units.⁷⁴ In 1988, the EU began to investigate anti-dumping charges brought against color televisions made in China and South Korea. The result of that investigation came out against the manufacturers, and an anti-dumping duty of 15.3% was levied on Chinese televisions beginning in 1991.⁷⁵

In 1992, the EU launched another investigation of imported televisions, which resulted in an anti-dumping tariff of 25.6% being imposed by the Council on Chinese sets beginning in March 1995.⁷⁶ Three years later, following the promulgation of the New Anti-dumping Rule, the EU decided that the existing tariff rate on imported sets would remain unchanged for most nations, but rise to 44.6% for those made in China.⁷⁷ Thus, for all intents and purposes, Chinese color televisions were expelled from the European market.⁷⁸

B. The Current Problematic Situation

In July 1998, the New Anti-dumping Rule entered into force, making significant legislative progress in the EU anti-dumping regime.⁷⁹ However, this has not been followed by the significant progress that many observers may have expected. The EU campaign against China has not been restrained, nor have

^{73.} See Commission Regulation 129/91, supra note 59; Council Regulation 2093/91, supra note 59.

^{74.} See Boob Tube, supra note 66.

^{75.} Council Regulation 2094/91, supra note 59, art. 2.

^{76.} Council Regulation 710/95 Imposing a Definitive Anti-Dumping Duty on Imports of Colour Television Receivers Originating in Malaysia, the People's Republic of China, the Republic of Korea, Singapore and Thailand and Collecting Definitively the Provisional Duty Imposed, art. 1(2), 1995 O.J. (L 73) 3, 11.

^{77.} Council Regulation 2584/98 Amending Regulation 710/95 Imposing a Definitive Anti-Dumping Duty on Imports of Colour Television Receivers Originating in Malaysia, the People's Republic of China, the Republic of Korea, Singapore and Thailand and Collecting Definitively the Provisional Duty Imposed, art. 1, 1998 O.J. (L 324) 1, 12.

^{78.} See Boob Tube, supra note 66.

^{79.} Council Regulation 905/98, supra note 38, art. 2.

the accused Chinese exporters/producers been afforded more beneficial treatment (ME status) in anti-dumping proceedings due to the 1998 amendments.

In 1999, the new anti-dumping initiations within the EU reached eighty-six, involving imports from twenty-nine non-Member States and covering thirty-two products.⁸⁰ Historically, this is the largest number of new initiations in comparison with any prior year, such as twenty-nine in 1998 or forty-five in 1997.⁸¹ Among those eighty-six anti-dumping initiations, twelve involved Chinese products, accounting for 13.95% of all new investigations in that year.⁸²

One important reason for such an increase of anti-dumping actions is related to the Asian financial crisis.⁸³ The crisis led to a decline in domestic consumption in South East Asia, and affected trade with countries traditionally exporting to this region. In turn, countries such as China were compelled to redirect exports into other available markets, mainly towards the U.S. and the EU.⁸⁴ In this context, reference is made to the increase in new investigations opened by the EU concerning China and Taiwan.

However, the Asian financial crisis is essentially an occasional circumstance that may not explain the whole story of the ongoing severe EU anti-dumping practices against China, and a continuous trend of such practices appears inevitable for the near future. Meanwhile, the introduction of the New Anti-dumping Rule to this field has not yet brought about a situation that would inspire optimism about prospects for less discrimination and greater fairness in EU policy and practice toward Chinese business.

From July 1998 to June 2000, there have been nine antidumping investigations concerning the implementation of the New Anti-dumping Rule with China, where twenty-seven æcused Chinese companies claimed ME treatment. In the end, only three of them were granted ME status, representing just over 10% of all companies making the ME petitions.⁸⁵

^{80.} Eighteenth Annual Report, supra note 7, at 122.

^{81.} Id. at 20.

^{82.} Id. at 124-26.

^{83.} See id. at 21.

^{84.} *Id*.

^{85.} See Commission Proposal, supra note 64, at 6.

The low success level of ME claims is not in line with the original expectations from both the EU and China. A main reason for such a significant failure is related to the ability of the claiming Chinese companies to meet the five criteria set forth in the New Anti-dumping Rule.⁸⁶ For the twenty-four companies who were refused ME treatment, the EU decided that they had failed to meet the five criteria due to the following facts: (1) "restrictions on selling on the domestic market;" (2) "significant state interference in decision-making;" (3) "absence of properly audited accounts;" (4) "significant distortions in costs as a result of previous state involvement in the company;" and (5) that "barter trade commonly exists." ⁸⁷

At this point, we can see that the Chinese steel industry has been a typical case. In May 1999, the Commission initiated an investigation within the EU regarding "hot rolled . . . non-alloy" steel imported into the European market by China, Romania and India, resulting in an imposition of anti-dumping duties. The case was remarkable at the time, for it was the first large-scale test case of the New Anti-dumping Rule which recognized China's gradual transition to a market economy. To challenge the EU's orthodox dumping formulae, Brussels-based lawyers representing Chinese exporters invoked the right granted to Beijing and Moscow two years earlier by submitting price data from the Chinese domestic market rather than from a comparable reference country which exports the same product as was always the case before the New Anti-dumping Rule was introduced. So

Though the Commission's anti-dumping officials declared that they would never "take a soft or a tough line with the Chinese" since they were "technocrats," and would "take everything on a case-by-case basis," the result was rather frustration. All six Chinese companies claiming ME treatment in this case were refused, as the Commission decided that none of

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^{86.} See id. at 6-7.

^{87.} Id.

^{88.} Commission Decision 307/2000 Imposing a Provisional Anti-Dumping Duty on Imports of Certain Hot-Rolled Flat Products of Non-Alloy Steel Originating in the People's Republic of China, India and Romania, art. 1, 2000 O.J. (L 36) 4, 18. See also Peter Chapman, Chinese Steel Probe Will be Key Test of New Anti-Dumping Rules, Eur. Voice, May 1999, at 20, 26.

^{89.} See Chapman, supra note 88, at 26.

^{90.} *Id*.

those companies met the criteria on an individual basis, dthough as a group the six together demonstrated that all the criteria were in fact met.⁹¹ The Commission listed the reasons for its refusal as: (1) all companies were fully or partially owned by the state; (2) agreements existed to purchase raw materials from state owned suppliers; and (3) only nominal fees were paid for land-use rights under barter trade practices.⁹²

In May 2000, the Commission initiated another investigation against Chinese "fluorescent" lighting products, involving several hundred Chinese manufacturers.⁹³ Of the Chinese manufactures investigated through random sampling, only two were finally entitled to ME status and able to take advantage of their preferential tariff treatment.⁹⁴ Seven other Chinese companies were not so fortunate in receiving NME status, meaning their products would be subject to the high average tariffs.⁹⁵

C. Future Trends

From all that has been reviewed above, with rapid growth of China-EU trade relations, a continuous trend of the EU antidumping campaign against Chinese products is foreseeable in the next five to ten years (or even longer). The improvement of the EU instrument, to adhere to the changing reality of China's economy, may provide the accused Chinese industries more or less legal opportunity to defend against, and challenge this ongoing campaign, but not stop it. In addition, the entry of China into the World Trade Organization ("WTO") may help

^{91.} Commission Decision 307/2000, *supra* note 88, at 8. *See also* Commission Proposal, *supra* note 64, at 7.

^{92.} See Commission Proposal, supra note 64, at 7-8.

^{93.} Commission Regulation 255/2001 Imposing a Provisional Anti-Dumping Duty on Imports of Integrated Electronic Compact Fluorescent Lamps Originating in the People's Republic of China, 2001 O.J. (L 38) 8. See also EU Targets Chinese Light-Fixture Producers in Anti-Dumping Probe, China Online (Aug. 16, 2000), at http://www.chinaonline.com [hereinafter EU Targets].

^{94.} Commission Regulation 255/2001, supra note 93, at 10.

^{95.} Id. at 10-12.

^{96.} See Boob Tube, supra note 66.

^{97.} See Council Regulation 905/98, supra note 38, at 18.

^{98.} On November 10, 2001, the WTO's Ministerial Conference approved China's entry into the WTO. See Press Release, World Trade Organization, WTO Ministerial Conference Approves China's Accession (Nov. 10, 2001),

her gain international judicial remedies to the EU antidumping campaign under the international trade regime.⁹⁹ Realistically, however, China will never be able to wipe out the campaign.

IV. IMPACT OF THE EU ANTI-DUMPING CAMPAIGN ON CHINESE INDUSTRIES

The ongoing EU campaign against imports from China has invited growing concern from both Chinese export industries and the government in Beijing.¹⁰⁰ Since the full campaign began in 1988, it has created substantial, serious impacts on many aspects of the China's economy.¹⁰¹

A. A Most Visible and Direct Impact: Monetary Losses of Chinese Industries

Usually, the value of an anti-dumping case is so high that each percentage point of an anti-dumping margin can represent a significant annual cost to the company. In the case of Chinese industries involved, from 1990 to 1997, the import value of Chinese products subject to EU investigations amounted to roughly 100-200 million euros per year, corresponding to 1% of the total value of annual imports from China. In 1994, the import value of Chinese products subject to EU investigations or measures corresponded to roughly 1

 $available\ at\ \ http://www.wto.org/english/news_e/pres01_e/pr252_e.htm\ [hereinafter\ Press\ Release].$

^{99.} See Understanding on Rules and Procedures Governing the Settlement of Disputes, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 2, Legal Instruments-Results of the Uruguay Round vol. 31, 33 I.L.M. 1226 (1994), available at http://www.wto.org/english/tratop_e/dispu_e/dsu_e.htm (last visited Feb. 24, 2002) [hereinafter DSU].

^{100.} Yiwei Wang, *Philips De Yuandong Yinmo* [*Philips' Far-Eastern Conspiracy*], GUANGZHOU DAILY ONLINE (Sept. 22, 2000), at http://dailynews.sina.com.

^{101.} *Id*.

^{102.} See Christopher F. Corr, Trade Protection in the New Millennium: The Ascendancy of Antidumping Measures, 18 Nw. J. Int'l L. & Bus. 49, 103 (1997).

^{103.} Fu, *supra* note 5, at 76.

billion euros, or more than 4% of the total import value (23 billion euros) of Chinese products that year.¹⁰⁴

B. Another Visible and Direct Impact: Inferior Position of Chinese Exporters/Producers Within the European Market

An anti-dumping case may result in imposition of prohibitive company-specific import duties, thus placing the exporting company concerned at a competitive disadvantage (relative to domestic companies, as well as exporters from non-targeted countries). If the dumping duties are high enough, exporters can be excluded from the market entirely.¹⁰⁵

Suffering the EU anti-dumping campaign for more than ten years, quite a few Chinese industries, especially those who have strong competitive capability in the world market, have been severely damaged in their business, either losing significant market share or being expelled from the European market.¹⁰⁶ Among these victims, the Chinese television industry is a significant example.¹⁰⁷

Before 1993, the export of a single Chinese television manufacturer, XOCECO, to the EU had reached 300,000 sets a year. Until 1999, after experiencing a twelve-year EU antidumping campaign, the total export of the Chinese television industry to the EU market was just 30,000 sets. By now, the Chinese television industry has almost been excluded from the European market. An even earlier example is the Chinese bicycle industry. In 1991, China's export level reached 2,000,000 bicycles. After being hit with an anti-dumping duty of 30.6% in 1993, this industry was effectively expelled from the European market. China's fluorescent lights industry presents a more recent case. Shenzhen Zhongdian Lighting

^{104.} See id. at 76-77.

^{105.} See Corr, supra note 102, at 74.

^{106.} See Yiwei Wang, supra note 100.

^{107.} See Ma, supra note 3.

^{108.} Id.

^{109.} Id.

^{110.} *Id*.

^{111.} Xuezhong Wan, Zhongguo Chengwei Guoji Fan Qingxiao Zui Da Shouhaizhe [China has Become the Most Distinctive Victim in the International Anti-Dumping Practice], CHINA LEGAL DAILY (Aug. 8, 2000), at http://www.legaldaily.com.cn/gb/contents/2000-08/08/content_2886.htm.

^{112.} See Council Regulation 2474/93, supra note 60, art. 1.

Co. ("Shenzhen Zhongdian"), China's leading enterprise in this industry, exported lighting products worth almost USD \$40 million in 1999, with half of these products being exported to EU Member States. However, since May 17, 2000, when the EU initiated its investigation against this industry, Shenzhen Zhongdian's export orders have fallen daily, with the company's current daily export volume plummeting more than 60%. However, the same state of the same state of the same state of the same state of the same state.

What is more painful to the Chinese is that in numerous cases where their products were excluded from the European market as a result of the imposition of anti-dumping measures, the market shares previously held by Chinese exporters were simply replaced by the exports from other developing countries.¹¹⁵

C. The Longstanding, Profound Impact on Chinese Emerging Industries

In the EU anti-dumping practice, many targeted Chinese industries are emerging industries such as electronics and steel production, both vital to China's economic development. 116 Due to current EU law and practice, the conclusion of a single antidumping case against one or more individual Chinese companies may become a quasi-precedent for later cases against others in the same industry. Therefore, with respect to the European market, me conclusion in favor of the European complainant may threaten the exportation of the whole Chinese industry concerned. Also, the more such conclusions come out, the more European companies will be encouraged to abuse their anti-dumping rights against their Chinese counterparts.¹¹⁷ This creates an even more unfair and discriminatory circumstance in regard to Chinese products exported into the European market. As a result, not only will the emerging Chinese industries be damaged, but long-term China-EU trade relations will be undermined.

^{113.} See EU Targets, supra note 93.

^{114.} See Commission Regulation 255/2001, supra note 93; EU Targets, supra note 93.

^{115.} See Fu, supra note 5, at 104-105.

^{116.} See Boob Tube, supra note 66.

^{117.} See Fu, supra note 5, at 104.

D. The Long-Term, Negative Impact on China's Foreign Direct Investment

Since the 1980's, when China enacted its open policy and commenced economic reform, it has established an export-oriented economy and attracted tremendous foreign direct investment ("FDI"). Most of the Chinese exporters are foreign-investment enterprises. As the EU anti-dumping campaign becomes more and more severe concerning imports from China, there is a sharp decrease of exports and profits by these enterprises, which may discourage the foreign investors from continuing to invest in Chinese industries affected by the EU campaign. 119

No doubt, the ongoing EU campaign has led to serious negative effects at all levels of China's economy. As this campaign evidences a continuous trend, it is increasingly urgent and necessary for the Chinese industries concerned and China itself to develop a set of adequate and effective legal strategies of defense and challenge.¹²⁰

V. LEGAL STRATEGIES FOR CHINA TO CHALLENGE THE EU ANTI-DUMPING CAMPAIGN

As previously mentioned, the ongoing EU anti-dumping campaign against imports from China has not only resulted in serious negative impacts on the Chinese industries concerned, but has also become a large obstacle to the development of China-EU trade relations. To deal with that difficult situation, China and its enterprises need to develop adequate, effective legal strategies to defend and challenge where appropriate.¹²¹ In this context, efforts made by both business and government

^{118.} Shaun Breslin, "Made in China": The Growth of Chinese Trade 9-10 (Cent. for the Study of Globalization and Regionalisation, Working Paper No. 19/98, 1998), available at http://www.warwick.ac.uk/fac/soc/GSGR/wpapers/wp1998.pdf (last visited Feb. 24, 2002).

^{119.} See Wan, supra note 111.

^{120.} See Yingjie Guojihua Tiaozhan – Yingdui Oumeng Fan Qingxiao Yantaohui Lianhe Shengming [Joint-Declaration Upon the Seminar on Meeting International Challenges in Dealing with the EU Anti-Dumping Campaign], GUANGZHOU DAILY ONLINE (Sept. 22, 2000), at http://dailynews.sina.com [hereinafter Joint Declaration].

^{121.} See id.

are equally important, and both should work in tandem to accomplish their common goals.

A. Strategies for the Chinese Enterprises Concerned to Diminish or Avoid Anti-Dumping Liability

As direct victims of the EU anti-dumping campaign, targeted Chine se exporters/producers tangibly suffer the consequences of each EU investigation. So, it must be in their best interests to conduct a strong and effective defense against the dumping claims, to diminish or avoid liability. For this purpose, the Chinese enterprises concerned may want to consider the following strategies.

1. The Prompt and Effective Response to the EU Anti-Dumping Actions

When receiving an EU anti-dumping allegation, the Chinese enterprises involved should take a positive or even aggressive attitude, promptly and effectively responding to these actions. Many lessons learned through the experiences of Chinese industries repeatedly shows the correctness of this strategy.¹²²

In the past twelve years, most of the Chinese enterprises involved in the EU anti-dumping practice have taken a passive attitude on their own role. They either ignored or just remained silent concerning the anti-dumping initiations targeting them, considering the costly defense procedures, protection of operational secrets of the enterprises, or even a traditional idea that said "[s]helf it when it is none of my business." But it truly is their business.

The consequences of inaction have been tragic. With the lack of answers from the accused Chinese companies, in most cases, the EU directly imposed severe anti-dumping measures on Chinese products merely based on the available facts provided by the European companies. Gradually, many Chinese industries concerned were kicked out of the European market.¹²⁴

For instance, until 1999, during ten years of EU investigations and reviews into SCTVs and the Chinese television

^{122.} See Xiao Yu, China's TV Industry Answers EU Anti-Dumping Suit, CHINA ECON. WEEKLY (Aug. 25, 2000), at http://www.ultrachina.com.

^{123.} Id.

^{124.} See Boob Tube, supra note 66.

dumping matters, all accused Chinese enterprises in the television sector retreated into obscurity, no one standing up to answer the claims. During the television anti-dumping proceeding in 1998, in one of a series of consequences, the Council boldly raised the Chinese anti-dumping tax rate to 44%, and in effect excluded Chinese enterprises from the European market. In sharp contrast, Samsung Electronics Co., Ltd. and LG TeleCom of South Korea formed a strategic alliance during the case review, provided complete data for responding, lobbied through different channels, and defeated the claims they faced. With a 15.1% anti-dumping tax rate, South Korean firms easily occupied the market share previously enjoyed by the Chinese. 127

This example should persuade Chinese enterprises to take a positive (or even aggressive) attitude toward the role they play in EU anti-dumping investigations. Answering such allegations may be costly, but it will definitely cost more if they default in the case and do nothing. Every targeted Chinese exporter/producer should take the EU proceedings for what they are: efforts by EU producers to make foreign producers less competitive or shut them out of the European market altogether. A prompt and effective response to those actions would always be a good start for the Chinese exporters/producers to win the cases and discourage their European counterparts from further abuse of the anti-dumping instrument.

2. A Strong and Sound Defense

Of course, a good start does not mean ultimate success. Chinese enterprises should further conduct a strong and sound defense in line with the current EU anti-dumping instrument. After all, any EU anti-dumping proceeding would be subject to the jurisdiction of the Member State where the applicable law is the EU anti-dumping law.

^{125.} Yu, *supra* note 122.

^{126.} See Council Regulation 2584/98, supra note 77, art. 1.

^{127.} See Yu, supra note 122.

^{128.} See Edward A. Vermulst & Folkert Graafsma, A Decade of European Community Anti-Dumping Law and Practice Application to Imports from China, 26 J. World Trade 5, 42 (1992).

For this defensive purpose, Chinese companies concerned need to take full advantage of the current EU anti-dumping instrument for their own interest. First of all, they should develop a complete, accurate working knowledge of the EU rules, in the sense of both substance and procedure. Then, with the knowledge acquired, they may strategically apply the EU anti-dumping rules in favor of Chinese interests to build up an effective, strong defense. Below are presented several aspects of how to carry out this strategy.

Due to the nature of anti-dumping proceedings, accused Chinese enterprises should pay attention to the calculation of dumping margin (by which the existence of dumping and the anti-dumping rate are determined),¹²⁹ and try to minimize this margin in their respective cases. A calculation in favor of the Chinese companies can be conducted through a number of steps. First, the Chinese enterprises should seek full ME status by convincing the EU they fulfill the five criteria provided in the New Anti-dumping Rule.¹³⁰ Succeeding in doing so, the Chinese enterprises will be entitled to a normal methodology in the determination of dumping margin, which may minimize the margin the most.

When failing to obtain full ME status, Chinese enterprises may shift their efforts to pursuing a traditional individual treatment which is occasionally available to the accused companies under the EU regime.¹³¹ Individual treatment can contribute to minimizing the dumping margin of targeted Chinese enterprises, for their individual domestic export price will be taken into account, and their own comparative advantages in the European market (low labor cost, low material cost) will possibly be accepted for purpose of adjusting the margin as well.¹³²

However, the individual treatment does not exclude the application of an undesirable analogue country methodology in the determination of normal value.¹³³ The accused Chinese

^{129.} See Council Regulation 384/96, supra note 11, art. 2(11)-(12).

^{130.} See Council Regulation 905/98, supra note 38, art. 1.

^{131.} See Fu, supra note 5, at 81.

^{132.} See Wang, supra note 14, at 145.

^{133.} See Fu, supra note 5, at 81-82. In the case of SCTVs, "The individual dumping margin was, in this case, determined as a comparison between the

enterprises may still risk a high dumping margin. In light of this, how to choose an appropriate analogue country will still be a big concern.

As for those who neither obtain full ME status nor receive individual treatment, they may risk the highest dumping margin, since the EU can be expected to apply the most unfair and discriminatory anti-dumping policy to their cases, as it has done in the past to most of the accused Chinese companies. ¹³⁴ For these unfortunate enterprises, the only strategy available, in respect to dumping margin calculations, is to make certain that an appropriate analogue country is selected for determining normal value. It should be noted that calculation of dumping margin is merely one of the technical aspects of an antidumping proceeding. Though a vital part, it can never replace the functioning of the entire proceeding. So, if a Chinese enterprise fails to get credits in this part, it does not mean all is lost.

According to current EU law, anti-dumping measures shall not be imposed until the dumping causes material injury to EU products, such that the latter cannot compete on an equal footing with the foreign importers. This provides the accused a solid legal ground upon which there have been quiet a few Chinese companies released from the specter of adverse findings to avoid the anti-dumping liability. 136

During a twelve-year EU anti-dumping campaign against imports from China, there were quite a few accused Chinese exporters/producers released from liability for such reasons. In 1992, eight cases were initiated against Chinese products. ¹³⁷ Four of them, namely unwrought manganese, refined antimony trioxide, gum-rosin and paint brushes were terminated due to a lack of injury findings or because of lack of support by a majority of Member States. ¹³⁸

However, chances to avoid anti-dumping liability through the injury analysis are generally slim. First, the injury analysis

weighted-average normal value established in an analogue country and the individual export price charged by each Sino-Foreign joint-venture." *Id.*

^{134.} Id.

^{135.} See Council Regulation 384/96, supra note 11, art. 3.

^{136.} See Fu, supra note 5, at 104.

^{137.} Id.

^{138.} Id.

involves the examination of all relevant factors, such as: (1) increase of dumped import volumes; (2) sale price of the EU industries undercut; (3) decrease of production volumes of the EU industries; (4) market share loss; and (5) forced cutbacks of employees. Second, the Basic Regulation apparently favors the European complainants in this regard, by providing that dumped imports do not have to be the only cause of the injury to justify imposition of anti-dumping measures. Accordingly, burden of proof based on this analysis can often be overwhelming and prevent the accused from making a successful innocent argument.

According to Article 9(1) of the Basic Regulation, "Where the complaint is withdrawn, the proceeding may be terminated unless such termination would not be in the Community interest." This provision gives another legal ground for waiving the possible liability of the accused Chinese enterprises. A strategy designed on this ground should focus on how to persuade or push the European complainants to withdraw their complaints. An answer may lie in the advancing China-EU economic relations.

With economic ties growing rapidly, more and more European industries seek access to the broad and potentially lucrative Chinese market by exporting to China or establishing joint-venture companies with local Chinese enterprises. The more successful their businesses are in China, the more interests they will have linked to local Chinese industries. Interestingly, many European adventurers happen to be the major complainants in the EU anti-dumping proceedings against their present or potential Chinese partners. A feasible approach for the accused Chinese companies is to take advantage of their European counterparts' consideration of the balance of interests, and push the latter to withdraw their complaints.

Here, the Netherlands' Philips Electronics Co. ("Philips") is a typical example. It has been seventeen years since Philips es-

^{139.} Eighteenth Annual Report, supra note 7, at 13.

^{140.} Id. See also Council Regulation 384/96, supra note 11, art. 3(5)-(7).

^{141.} Council Regulation 384/96, supra note 11, art. 9(1).

^{142.} See Ma, supra note 3.

^{143.} See, e.g., Hooked on A Feeling: Philips to Examine EU's Anti-Dumping Policy on Chinese Color TVs, China Online (Sept. 6, 2000), at http://www.chinaonline.com [hereinafter Hooked on a Feeling].

tablished its first joint venture in China, in 1985.¹⁴⁴ Today, the European electronic giant owns more than thirty solely funded enterprises and joint ventures with investments topping USD \$1 billion in China.¹⁴⁵ It has taken a considerable share of the Chinese electronic home appliance and mobile phone markets with the slogan "Let's make it better."¹⁴⁶ Meanwhile, however, Philips has been a major complainant in a series of antidumping cases against Chinese electronic products in the past nine years.¹⁴⁷

In August 2000, when Philips sought a partnership with China's Changhong Electronic Co. ("Changhong"), its attempts were hurt by revelations of its role in an EU anti-dumping campaign against Chinese manufacturers of color televisions, including Changhong. After Philips' role was disclosed in April 2000, its efforts to obtain a partnership with the Chinese company "disgusted" Chinese consumers – especially because Philips had been prospering in the Chinese market itself. Not only did the Chinese television industry strongly resist further business cooperation, but it was also reported that the Chinese public severely criticized Philips' "immoral" behavior. 49

Currently, some experts in the legal community suggest that Chinese television makers take advantage of Philips' desire to restore and improve its commercial image destroyed by this incident, and persuade the company to withdraw its complaints. These experts regard the approach as the most practical for the accused Chinese manufacturers to settle the cases without loss, as it is estimated there would be only a 10% chance that the enterprises would win the cases once both sides go before the Commission. 151

As for Philips, it has been previously unwilling to negotiate. However, between May and June 2000, it actively conducted long negotiations with Chinese parties.¹⁵² A Philips top execu-

^{144.} Id.

^{145.} Id.

^{146.} Yu, *supra* note 122.

^{147.} See Hooked on a Feeling, supra note 143.

^{148.} EU Lawsuit Making Philips' China Color TV Partnership Difficult, CHINA ONLINE (Aug. 14, 2000), at http://www.chinaonline.com.

^{149.} Id.

^{150.} Yu, supra note 122.

^{151.} Ma, *supra* note 3.

^{152.} Yu, supra note 122.

tive told the Chinese public that his company was already aware of the problem, and would be taking measures to solve it as soon as possible.¹⁵³

3. The Capacity to Handle Anti-Dumping Proceedings

Above, the author has listed a few legal undertakings to enable Chinese enterprises to win EU anti-dumping cases. Accomplishment of these legal goals depends on the good performance of trade lawyers hired by the investigated companies. However, by no means can the accused companies disregard their own substantive role in the cases. Without showing a good capacity for handling these issues, the accused will still encounter many difficulties with their cases.

Take the instance of an ME status claim. In the EU proceedings against imports from China, when the accused Chinese company claims ME status, it is required to meet the burden of proof for the five criteria discussed previously.¹⁵⁵ To prove the fulfillment of these criteria, the company has to provide a great deal of information, from private managing and operating decisions, accounting records, production costs and financial situations to exchange rates and the public legal environment of its home country. Gathering and selecting this information requires tremendous daily work conducted by the company itself, in advance. Also, each submitted document requires a translation into English. This job alone can be very time consuming. In a word, one cannot expect all these preparations to be done overnight.¹⁵⁶

In addition, according to the Basic Regulation, deadlines for an anti-dumping investigation remain fixed, so that an ME status claim has to be dealt with extremely quickly in order to meet these deadlines.¹⁵⁷ A special claim form should be completed and returned to the Commission within three weeks of

^{153.} See Hooked on a Feeling, supra note 143.

^{154.} See Joint Declaration, supra note 120.

^{155.} See Council Regulation 905/98, supra note 38, art. 1.

^{156.} See Overview of the Monitoring of Third Country Safeguard Cases and of the Implementation of the Trade Barriers Regulation: Seventeenth Annual Report from the Commission to the European Parliament on the Community's Anti-Dumping and Anti-Subsidies Activities, COM(99)411 final at 7–8 [hereinafter Seventeenth Annual Report].

^{157.} See id. at 7.

the initiation of a proceeding. In this form, a minimum amount of information is required, which is needed to decide whether or not a concerned Chinese company is operating in a market economy environment (five criteria).¹⁵⁸ Due to the tight deadlines, both the criteria and the timeframes are applied strictly. If any information is missing in the completed claim form, or if it is returned late, the claim is automatically rejected.¹⁵⁹

For these reasons, accused Chinese companies should strengthen their capacity to perform the comprehensive work required by the EU proceedings. The key issue here is to create a corporate structure ready for any possible anti-dumping challenge. In this context, a company may want to establish the following structures: (1) "sales personnel, to enforce price guidelines and review sales and selling expense information;" (2) "accounting personnel, to collect and derive the necessary cost, expense and sales information from the corporate, divisional and factory levels;" (3) "computer personnel, to arrange and maintain necessary data, and to run the dumping margin analysis;" and (4) "adoption of the EU competition law." 160

Like an old Chinese saying says: "Attack is the best defense." Thus the accused Chinese companies may also try another approach to make the anti-dumping initiations void – to invoke the EU competition law due to an inherent controversy between the anti-dumping law and competition law.¹⁶¹

This strategy seems very tricky, but is truly feasible! An interesting case may convince Chinese companies of this. In the late 1990's, European stainless steel bar producers filed a dumping complaint against Indian counterparts, putting the latter under dumping investigation. Soon after, Indian producers filed a complaint as well, asserting that the European bar producers had unlawfully fixed prices. As a result, the EU launched a price fixing investigation. Such a situation raised an important question as to the EU's anti-dumping practice:

^{158.} See id.

^{159.} See id. at 8.

^{160.} Corr, *supra* note 102, at 106.

^{161.} See Peter J. Koenig, Hot Topics in Dumping Law and Steel, Paper Presented to Metal Bulletin's Eastern European Steel Conference (May 27-29, 1998), at http://ablondifoster.com/library/article.asp?pubid=94359792001 &groupid=12.

^{162.} Id.

Whether imports should be found dumped and injurious on the basis of depressing EU prices when those prices had been unlawfully fixed?¹⁶³ Obviously the answer should be "no."

4. Adoption of the Chinese Anti-Dumping Instrument

Anti-dumping is a traditional and commonly used weapon in worldwide trade wars. Industries of many nations often adopt their own domestic anti-dumping instruments to restrain the anti-dumping campaigns launched by foreign competitors. ¹⁶⁴ However, to many Chinese companies that have suffered severely at the hands of foreign investigations, this weapon is too new to be handled freely.

Not until 1997 did China formulate her first anti-dumping legislation, the Anti-Dumping and Anti-Subsidies Regulations of the People's Republic of China ("Anti-Dumping and Anti-Subsidies Regulations"). Since then, there have been few Chinese industries adopting this domestic instrument to combat the anti-dumping campaigns from foreign economies, including the EU. 166

Under the current situation, where an increasing number of leading European industries are seeking access to broad and potentially lucrative Chinese markets, their business interests become increasingly linked to China. Any Chinese domestic anti-dumping initiation targeting European adventurers may constitute a heavy form of pressure on the latter. So, there is no reason why suffering Chinese companies cannot take full advantage of new domestic instruments to restrain their European counterparts from abusing the rights under EU anti-

164. Doreen Bekker, China and Antidumping Legislation, Paper Presented at the Economic Society of South Africa's Conference (Sept. 6-7, 1999) (on file with Journal).

¹⁶³ *Id*

^{165.} Zhonghua Renmin Gongheguo Fanqingxiao He Funbutie Tiaoli (Anti-Dumping and Anti-Subsidy Regulations of the People's Republic of China), ch. I, translated in China L. for Foreign Bus. Reg. (CCH) ¶¶ 19-620–19-620(42) (Aug. 26, 1997).

^{166.} See Kermit Almstedt & Patrick M. Norton, China's Antidumping Laws and the WTO Antidumping Agreement, 34 J. World Trade 75, 75-76 n.4-5 (2000). By 2000, among the five anti-dumping investigations undertaken by China on imports of newsprint, steel and chemical products, three received final rulings and one received a preliminary ruling. Id.

^{167.} See Hooked on Feeling, supra note 143.

dumping law. Of course, this strategy needs strong support from the Chinese government. Below, the author discusses in more detail the role of Beijing in fighting the EU campaign.

B. Strategies for the Chinese Government to Challenge EU Anti-Dumping Law and Practice

The Chinese government plays an independent and vital role in its discretion to challenge the EU anti-dumping campaign against imports from China. China's objective is to support, assist and guide domestic industries concerned with winning this legal contest. Generally, the Ministry of Foreign Trade and Economic Cooperation ("MOFTEC") is the main governmental organ in charge in this field. In recent years, other quasi-governmental organizations have also played an active role on this front, such as the Import and Export Chamber and the Foreign Investment Society. They make it the emphasis of their work to systematically organize Chinese enterprises concerned with such an onslaught. Currently, there are several strategies available to China in accomplishing its objective regarding the anti-dumping fight.

1. Imposing Political Pressures

The inflexibility of the EU anti-dumping legislation is a long-standing problem that contributes to the continuous trend of campaigns against China. Development of new law within the EU advances very slowly due to internal bureaucratic operations. Such legislative lethargy pays no heed to the fascinating changes happening in today's China.

Expecting a fundamental change in this field, China should urge the EU to adjust its anti-dumping instrument in light of the changing reality of China's economy, by amending the current regulations in a timely and efficient manner. External political pressure can be a good shortcut to that end. The New

^{168.} For more information on MOFTEC, visit its official website at http://www.moftec.gov.cn/moftec_en/index.html (last visited Feb. 24, 2002). 169. See Yu, supra note 122.

^{170.} See Sean C. Monoghan, Comment, European Union Legal Personality Disorder: The Union's Legal Nature Through the Prism of the German Federal Constitutional Court's Maastricht Decision, 12 EMORY INT'L L. REV. 1443, 1474-75 (1998).

Anti-dumping Rule is a successful example where, under the political pressure from China, the EU was forced to update its rules on regulation of imports from NME countries, including China.¹⁷¹ In sum, by gaining as many bids as possible from the rapid growth of China-EU trade relations, and the increasing interests attached to the Chinese market by European companies, Beijing may take a firm stance to impose more political pressure on the EU in bilateral negotiations. This can help push EU law and practice in a new direction that will diminish their discriminatory and unfair impacts on China.

2. Implementing Pragmatic Trade Policies

For many years, Western countries consistently criticized China for her "trade protectionism" practice.¹⁷² However, facing a severe anti-dumping campaign from the EU, China may have to strengthen the implementation of its protective trade policy, launching appropriate trade retaliations to challenge this campaign. In particular, under the current situation where the EU rarely adjusts its anti-dumping instrument in favor of China, while European industries frequently adopt this instrument to strike at their Chinese competitors, the strategy of taking pragmatic trade retaliation is likely to appear reasonable and workable to the Chinese government.¹⁷³

The recent case of the China-Korea "garlic war" may have already convinced Beijing of the benefits of this strategy. 174 From 1998 to 1999, with a dramatic increase in China's exports of garlic to the Korean market from 3.4% to a whopping 35%, the Korean government simply increased the import tariff from 35% to an astronomical 315%. 175 Correspondingly, China retaliated and banned Korean imports of polyethylene and cellular phones – two of Korea's major export items. This garlic trade war ended in a compromise after two weeks of intense

^{171.} See Eighteenth Annual Report, supra note 7, at 16-17.

^{172.} U.S. Trade Representative, 2001 National Trade Estimate Report on Foreign Trade Barriers 42 (2001), available at http://www.ustr.gov/html/2001 contents.html (last visited Feb. 24, 2002).

^{173.} See Eighteenth Annual Report, supra note 7, at 16-17; Seventeenth Annual Report, supra note 156, at 6-7.

^{174.} Caroline Cooper, End of Garlic War Brings Korea Potpourri of Good News, China Online (Aug. 14, 2000), at http://www.chinaonline.com. 175. Id.

negotiations between the two countries, with Korea agreeing to set certain "quotable tariff" levies upon imported Chinese garlic. 176

We may wonder if there is any significant difference between the EU and Korea regarding their importance in China's foreign trading. The big difference is that China's trade retaliation against the EU can invite a more severe revenge from the EU, and ultimately lead to more serious damage to the Chinese industries in the European market.¹⁷⁷ We must remember, however, that the health of China-EU trade relations can only be guaranteed on a reciprocal basis; a primary threshold for both sides to mutually benefit in their trade relations. It must be in the fundamental interests of China, and ultimately, the cause of free trade, for Beijing to adopt a trade policy instrument to challenge the unfair, discriminatory anti-dumping campaigns from abroad, including EU. Trade retaliations may be a worthwhile strategy for the Chinese under the present circumstances.

3. Improving the Chinese Regime

As we may realize, with a reciprocal approach, other than a legitimate one that is recognized by the international trading forum (the WTO), trade retaliations are just a tentative technique to cope with the EU anti-dumping campaign.¹⁷⁸ A better strategy may be for China to make efforts to improve its domestic regime, which is currently supported by a single statute, the Anti-Dumping and Anti-Subsidies Regulations. That law is just a copy of those that exist in certain Western countries, failing to reflect the reality of China's anti-dumping situation. As

^{176.} Id.

^{177.} Ma, supra note 3.

^{178.} It was not until May 1994, when the government promulgated the Foreign Trade Law of the People's Republic of China, that the country applied the reciprocity principle of the GATT to resolutions of Chinese trade disputes with other countries. See Zhonghua Renmin Gongheguo Duiwai Maoyi Fa (Foreign Trade Law of the People's Republic of China) art. 7, translated in Legislative Affairs Comm'n of the Standing Comm. of the Nat'l People's Congress of the People's Republic of China, The Laws of the People's Republic of China 1994, at 29-37 (1996). According to Article 7, the government should undertake appropriate counter measures against any countries or territories that apply discriminatory trade bans or trade restrictions against China. Id.

a source of law, the regulations are too abstract and general to be effective.

To improve the domestic regime, Beijing has been working on formulating a new law to address the abuse of anti-dumping by foreign enterprises, so as to impose sanctions in China's domestic market against those who, using unequal methods, hinder Chinese exports abroad.¹⁷⁹ Hopefully this law will successfully codify the balanced approach advocated here.

4. Taking Advantage of the Recent WTO Membership

All three strategies mentioned above are either at the unilateral or bilateral level. Today, as China has recently entered the WTO,¹⁸⁰ the government may think about taking advantage of its membership to resolve the problem of the ongoing EU investigations.

In fact, the EU already takes into account China's WTO membership within its legislation. The Proposal for a Council Regulation Amending Regulation 384/946 suggested that "[o]n the basis that membership of the WTO indicates a certain level of economic reform and trade liberalization, it is proposed to extend the [ME] regime to those NME countries who are members of the WTO, and to automatically extend it to others when they become WTO members in the future."¹⁸¹

To apply the Basic Regulation to China's entry into the WTO, the Commission further suggested an amendment:

In antidumping investigations concerning . . . the People's Republic of China . . . which is a member of the WTO at the date of the initiation of the investigation, normal value will be determined in accordance with paragraphs 1 to 6, if it shown, on the basis of properly substantiated claims by one or more producers . . . and in accordance with the criteria and procedures set out in subparagraph (c) that market economy conditions prevail for this producer or producers in respect of the manufacture and sale of the like product concerned. When

^{179.} Recently, the new Anti-Dumping Regulation of the People's Republic of China entered into force on January 1, 2002. *See* Zhonghua Renmin Gongheguo Fanqingxiao Tiaoli (Anti-Dumping Rules of the People's Republic of China), *available at* http://www.cacs.gov.ch/new/wto/wto01.htm (last visited Mar. 7, 2002).

^{180.} See Press Release, supra note 98.

^{181.} Commission Proposal, supra note 64, at 15.

this is not the case, the rules set out under subparagraph (a) shall apply. 182

However, we may notice that this prospective amendment does not lead to any substantial change in current EU antidumping legislation concerning China. The case-by-case approach will remain the same as before, regardless of China's membership in the WTO, which will not necessarily mean China's coveted classification as an ME country. Therefore, it is predictable that WTO membership will not be very helpful for the accused Chinese enterprises aiming to gain full ME status in the EU proceedings.

For this reason, China should pay most of its attentions to another main aspect of the WTO – its dispute settlement mechanism. With China's entry into the WTO, it is now able to invoke the Dispute Settlement Mechanism of the WTO to challenge EU anti-dumping legislation and practice not in her favor – just as the EU has long been doing against its trading partners. In this way, China will be entitled to resolve the problem of the anti-dumping campaign at a more advanced multilateral level.

It is notable that, whatever strategy China may use, it should embrace a strong awareness of serving domestic enterprise and industry, working closely with them to guide, support and assist their move to challenge the EU anti-dumping campaign.

VI. CONCLUSION

Today, as China is increasingly integrating into the global economy and opens its doors to the world, China-EU trade relations may become strengthened and extended to a new level. When increasing numbers of Chinese enterprises begin seeking access to the European market, the ongoing EU anti-dumping campaign can constitute a huge obstacle. Frustrated by this

^{182.} *Id.* at 21.

^{183.} See DSU, supra note 99, art. 1.

^{184.} On August 28, 2000, the WTO Appellate Body upheld a Dispute Settlement Panel ruling against the United States Anti-dumping Act of 1916. As one of the parties to the case, the EU had been playing a very active role in challenging this legislation. See WTO Appellate Body Report on United States Anti-Dumping Act of 1916, WT/DS136/AB/R, WT/DS162/AB/R (Aug. 28, 2000), at http://www.wto.org.

campaign, not only will the international market exploration by Chinese industries become empty talk, but the health of China-EU trade relations will also be severely undermined. This consequence is good for neither China nor the EU. In particular, excessive anti-China trade restrictions by the EU tends to worsen the domestic dislocations and resultant human suffering in China, the country with the world's largest population.

The reality is that China has become one of the most significant targets, and also one of the most distinctive victims, of the EU anti-dumping campaign. This situation is manifest in a continuous trend, and will not be repaired in the short run. Facing such a truth, China and its industries should work closely to develop adequate and effective legal strategies to challenge this campaign. A positive attitude is important, while the right approaches are necessary. At this moment, the road ahead remains long and winding.