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**INDONESIA – RECOURSE TO ARTICLE 22.2 OF THE DSU IN THE
US – CLOVE CIGARETTES DISPUTE**

REQUEST FOR CONSULTATIONS BY THE EUROPEAN UNION

The following communication, dated 13 June 2014, from the delegation of the European Union to the delegation of Indonesia and to the Chairperson of the Dispute Settlement Body, is circulated in accordance with Article 4.4 of the DSU.

My authorities have instructed me to request consultations with the Government of the Republic of Indonesia ("Indonesia") pursuant to Articles 1 and 4 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU") and Article XXII:1 of the *General Agreement on Tariffs and Trade 1994* ("GATT 1994") with particular respect to Indonesia's unilateral recourse to Article 22.2 of the DSU in the context of the compliance and arbitration panel proceedings in Case DS406 *US – Clove Cigarettes*, and the exclusion of third parties from those proceedings. We consider this to be inconsistent with Articles 21.5, 22.2, 23.1 and 23.2(a) of the DSU, as well as Articles 10.1, 10.2 and 10.3 of the DSU. As the Appellate Body has clearly stated:

... before obtaining the DSB's authorization to suspend concessions, a Member must initiate a dispute settlement process in which it challenges the consistency with the covered agreements of a measure taken by another Member. The Member initiating the process will only be authorized to suspend concessions when the measure is found by the panel (and the Appellate Body, if appealed) to be inconsistent with the covered agreements and the Member taking the measure fails to implement the panel's (or Appellate Body's) findings within a reasonable period of time or, if it takes a measure to comply, that measure is found by the panel (and the Appellate Body) in compliance proceedings not to have brought the Member concerned into compliance. In other words, the Member will only be able to suspend concessions pursuant to the DSB's authorization after having had extensive recourse to, and abided by, the rules and procedures of the DSU, consistent with the requirements of Article 23.1.¹

Background to the dispute

At its meeting on 24 April 2012 the Dispute Settlement Body (DSB) adopted the Appellate Body Report on *United States – Measures Affecting the Production and Sale of Clove Cigarettes* (WT/DS406/AB/R) and the Panel report (WT/DS406/R), as modified by the Appellate Body Report.² Following the recommendations from the Panel and Appellate Body, the DSB requested the United States to bring its measure, found in the Appellate Body Report and in the Panel Report as modified by the Appellate Body Report, to be inconsistent with the TBT Agreement, into conformity with its obligations under that Agreement.³ Pursuant to Article 21.3(b) of the DSU, Indonesia and the United States agreed that the reasonable period of time for the United States to comply would be 15 months from 24 April 2012, expiring on 24 July 2013.⁴

¹ Appellate Body Report, *US-Continued Suspension*, para. 374.

² Action by the Dispute Settlement Body, WT/DS406/9, 1 May 2012.

³ Panel Report, *US – Clove Cigarettes*, para. 8.6; Appellate Body Report, *US – Clove Cigarettes*, para. 299.

⁴ Agreement under Article 21.3(b) of the DSU, WT/DS406/10, 19 June 2012.

On 23 July 2013 the United States informed the DSB and all WTO Members that, in the opinion of the United States, it had complied with the recommendations and rulings of the DSB following the original proceedings.⁵ On 12 August 2013 Indonesia informed the DSB and all WTO Members that, in the opinion of Indonesia, the United States had failed to bring the measure found to be inconsistent with the covered agreements into compliance therewith or to otherwise comply with the recommendations and rulings within the reasonable period of time, and that no satisfactory compensation had been agreed.⁶ Consequently, there is a disagreement between the United States and Indonesia as to the existence or consistency with a covered agreement of measures taken to comply with the recommendations and rulings, as provided for in Article 21.5 of the DSU.⁷ Article 21.5 provides that such a compliance dispute shall be decided through recourse to the procedures set out in the DSU, including, wherever possible, resort to the original panel.

Notwithstanding the disagreement with respect to compliance, on 12 August 2013, Indonesia requested authorisation from the DSB to suspend the application to the United States of concessions or other obligations under the covered agreements, pursuant to Article 22.2 of the DSU.⁸ The United States objected to the level of suspension proposed and claimed that the principles and procedures set forth in Article 22.3 had not been followed.⁹ The DSB agreed that the matter was referred to arbitration, as required by Article 22.6 of the DSU.¹⁰

At the DSB meeting on 23 August 2013 the representative of the European Union made the following statement:

The representative of the European Union said that the EU noted the statement made by the United States that it had taken measures to comply with the DSB's recommendations and rulings. The EU also noted that Indonesia did not agree that the United States had brought its measures into compliance with the TBT Agreement. It appeared that "there is a disagreement as to the existence or consistency with a covered agreement of measures taken to comply with the recommendations and rulings" of the DSB within the meaning of Article 21.5 of the DSU. The EU wished to recall that, pursuant to that provision, "such dispute shall be decided through recourse to these dispute settlement procedures, including wherever possible recourse to the original panel". In cases of disagreement about the existence or consistency with WTO rules of compliance measures, concessions or other obligations may be suspended under the DSU once there was a multilateral determination on the alleged compliance action. The EU hoped that the United States and Indonesia would ensure that the DSU procedures with regard to compliance and suspension of obligations in this dispute could be conducted efficiently and in the right sequence. Finally, the EU recalled that it had participated as a third party in the Panel and appeal proceedings in this dispute and, therefore, pursuant to Article 10, paragraphs 1, 2 and 3 of the DSU, it reserved its right to participate as a third party in any subsequent proceedings, including with respect to any disagreement as to the existence or consistency with a covered

⁵ Minutes of the DSB Meeting of 23 July 2013, WT/DSB/M/334, 2 October 2013, para. 1.45: "... these actions by the US health authorities brought the United States into compliance with the DSB's recommendations and rulings in this dispute within the reasonable period of time for compliance, which expired on 24 July 2013."; Minutes of the DSB Meeting of 23 August 2013, WT/DSB/M/335, 4 October 2013, para. 1.8: "... as the United States had notified the DSB at the 23 July 2013 meeting, the United States had complied with the recommendations and rulings in this dispute."

⁶ Recourse to Article 22.2 of the DSU by Indonesia, WT/DS406/12, 13 August 2013, page 1: "The United States failed to implement the recommendations and rulings of the DSB with respect to Section 907(a)(1)(A) by the end of the reasonable period of time, and no mutually acceptable arrangement for compensation has been reached. ... "; Minutes of the DSB Meeting of 23 August 2013, WT/DSB/M/335, 4 October 2013, para. 1.3 "... the US failure to comply with the DSB's rulings and recommendations in the Clove Cigarette dispute. ...".

⁷ Article 21.5 of the DSU provides in relevant part: "Where there is disagreement as to the existence or consistency with a covered agreement of measures taken to comply with the recommendations and rulings such dispute shall be decided through recourse to these dispute settlement procedures, including wherever possible resort to the original panel."

⁸ Recourse to Article 22.2 of the DSU by Indonesia, WT/DS406/12, 13 August 2013.

⁹ Recourse to Article 22.6 of the DSU by the United States, WT/DS406/13, 23 August 2013.

¹⁰ Minutes of the DSB Meeting of 23 August 2013, WT/DSB/M/335, 4 October 2013, para. 1.13.

agreement of measures taken to comply with the DSB's recommendations and rulings.¹¹

By communication dated 2 September 2013 the WTO Members were informed that the matter referred to the compliance/arbitration panel would be dealt with by the original panel, pursuant to Article 22.6 of the DSU.¹²

By communication dated 4 September 2013 the European Union requested that appropriate provision be made in the Working Procedures and Timetable of the compliance/arbitration panel proceedings in order to facilitate the exercise by the European Union of its third party rights in this dispute.

By communication dated 18 December 2013 the compliance/arbitration panel informed the European Union of its decision, taking into account the views expressed by Indonesia, not to accord the European Union third party rights in the compliance/arbitration panel proceedings.

The compliance/arbitration panel has not informed WTO Members that the compliance/arbitration proceeding has been suspended.

At the DSB meeting on 22 January 2014 the EU made a statement explaining that it considered that there had been a breach of its third party rights, and that what had occurred was inconsistent with Articles 22.2, 23.1 and 23.2(a) of the DSU, which was followed by a discussion.¹³ The European Union subsequently requested the circulation of a communication explaining its point of view,¹⁴ which was also discussed at the following regular DSB meeting on 26 February 2014.¹⁵

The First Written Submission of the United States of America in the compliance/arbitration panel proceedings (19 December 2013) devotes the first 39 of its 55 pages to explaining that the United States has fully implemented the recommendations and rulings of the DSB. Similarly, the US Responses to the compliance/arbitration panel questions in advance of the substantive meeting (11 March 2014), the US Opening Oral Statement (27 March 2014) and the US Responses to the compliance/arbitration panel questions following the substantive meeting (10 April 2014)¹⁶ all demonstrate that compliance proceedings are in progress.

The measures at issue

The measures at issue are Indonesia's decision to have recourse to Article 22.2 of the DSU and its request to that effect, as evidenced by WT/DS406/12, notwithstanding the existence of a disagreement with the United States as to compliance, together with Indonesia's omission in not initiating and pursuing compliance proceedings pursuant to Article 21.5 and Indonesia's omission in not requesting and procuring suspension of the arbitration panel proceedings pending the outcome of the compliance panel proceedings.

The measures at issue also include Indonesia's request that the European Union be unlawfully excluded from the compliance/arbitration panel proceedings, which was a genuine and substantial cause of that exclusion, as evidenced by the communication dated 18 December 2013 from the compliance/arbitration panel.

Any act or omission attributable to a WTO Member may be a measure for the purposes of WTO dispute settlement.¹⁷ The measures referred to by the European Union are acts or omissions attributable to Indonesia.

¹¹ Minutes of the DSB Meeting of 23 August 2013, WT/DSB/M/335, 4 October 2013, para. 1.10.

¹² Recourse to Article 22.6 of the DSU by the United States, Constitution of the Arbitrator, WT/DS406/14, 2 September 2013.

¹³ Minutes of the DSB Meeting of 22 January 2014, WT/DSB/M/341, 25 April 2014, paras. 8.1-8.20.

¹⁴ WT/DS406/15, 14 February 2014.

¹⁵ Minutes of the DSB Meeting of 26 February 2014, WT/DSB/M/342, 16 May 2014, paras. 5.1-5.22.

¹⁶ All documents available at: <http://www.ustr.gov/node/6356> (last visited on 28 May 2014).

¹⁷ Appellate Body Report, *US-Corrosion-Resistant Steel Sunset Review*, para. 81: "... any act or omission attributable to a WTO Member can be a measure of that Member for purposes of dispute settlement proceedings."

A WTO Member bringing a case under the DSU does not have to demonstrate any special interest over and above the fact of a WTO inconsistency.¹⁸ The measures at issue are WTO inconsistent for the reasons set out below. In any event, in this particular case, the European Union was a third party in the original panel proceedings and a third participant in the original Appellate Body proceedings. In addition, the European Union is engaged in the production, trade and regulation of cigarettes, including the types of cigarettes that have been referenced in this case. Furthermore, the European Union has a systemic interest in the correct and consistent interpretation and application of the covered agreements, also and particularly with respect to any suspension of concessions and possible effects on the European Union, including trade deflection or diversion effects. We have a close interest in these compliance/arbitration panel proceedings.

The WTO inconsistency of the measures at issue

Article 21.5 of the DSU¹⁹ refers to a situation where there is disagreement as to the existence or consistency with a covered agreement of measures taken to comply with the recommendations and rulings of the DSB. In these circumstances, this provision unconditionally provides for the obligation to have recourse to the dispute settlement procedures of the DSU ("*such dispute shall be decided through recourse to these dispute settlement procedures, including wherever possible resort to the original panel*").

Articles 21.5 and 22²⁰ indicate that Article 22 is premised on a situation of non-compliance, which the Appellate Body has indicated must be based on a multilateral determination to that effect. In this context, Indonesia's request for authorization from the DSB to suspend the application to the United States of concessions or other obligations under the covered agreements, pursuant to Article 22.2 of the DSU, together with Indonesia's omission in not initiating and pursuing compliance proceedings pursuant to Article 21.5 and its omission to request and procure suspension of the arbitration panel proceedings, was premised, by operation of law, on the proposition that the United States has failed to bring the measure found to be inconsistent with a covered agreement into compliance therewith or otherwise comply with the recommendations and rulings within the reasonable period of time determined pursuant to paragraph 3 of Article 21. However, there has not yet been any multilateral determination on the question of compliance. Rather, as recalled above, there is a disagreement between the United States and Indonesia as to the existence or consistency with a covered agreement of measures taken to comply with the recommendations and rulings, as provided for in Article 21.5 of the DSU.

Article 22.6 of the DSU²¹ is premised on the situation described in paragraph 2 occurring. The situation in paragraph 2 includes a situation in which the Member concerned has failed to comply,

¹⁸ Appellate Body Report, *EC – Bananas III*, paras. 132-138.

¹⁹ Article 21.5 of the DSU provides as follows: "Where there is disagreement as to the existence or consistency with a covered agreement of measures taken to comply with the recommendations and rulings such dispute shall be decided through recourse to these dispute settlement procedures, including wherever possible resort to the original panel. The panel shall circulate its report within 90 days after the date of referral of the matter to it. When the panel considers that it cannot provide its report within this time frame, it shall inform the DSB in writing of the reasons for the delay together with an estimate of the period within which it will submit its report."

²⁰ Article 22.2 of the DSU provides as follows: "If the Member concerned fails to bring the measure found to be inconsistent with a covered agreement into compliance therewith or otherwise comply with the recommendations and rulings within the reasonable period of time determined pursuant to paragraph 3 of Article 21, such Member shall, if so requested, and no later than the expiry of the reasonable period of time, enter into negotiations with any party having invoked the dispute settlement procedures, with a view to developing mutually acceptable compensation. If no satisfactory compensation has been agreed within 20 days after the date of expiry of the reasonable period of time, any party having invoked the dispute settlement procedures may request authorization from the DSB to suspend the application to the Member concerned of concessions or other obligations under the covered agreements."

²¹ Article 22.6 of the DSU provides as follows: "When the situation described in paragraph 2 occurs, the DSB, upon request, shall grant authorization to suspend concessions or other obligations within 30 days of the expiry of the reasonable period of time unless the DSB decides by consensus to reject the request. However, if the Member concerned objects to the level of suspension proposed, or claims that the principles and procedures set forth in paragraph 3 have not been followed where a complaining party has requested authorization to suspend concessions or other obligations pursuant to paragraph 3(b) or (c), the matter shall be referred to arbitration. Such arbitration shall be carried out by the original panel, if members are available, or by an arbitrator²¹ appointed by the Director-General and shall be completed within 60 days after the date of expiry of the reasonable period of time. Concessions or other obligations shall not be suspended during the course of the arbitration." (footnote omitted)

and, in case of disagreement, that there has been a multilateral determination to that effect. Article 22.7 of the DSU²² provides for a determination to be made as to whether the level of the concessions or other obligations to be suspended is equivalent to the level of nullification or impairment, whether the proposed suspension is allowed under the covered agreement, and whether the principles and procedures set forth in paragraph 3 of Article 22 of the DSU have been followed. In this case, these tasks are also to be carried out by the original panel. Thus, Articles 22.3-22.8 as a whole are premised on a situation of non-compliance. They all refer directly or indirectly to the nullification or impairment arising from non-compliance. If the DSB would, pursuant to Article 22.7 of the DSU, by negative consensus or automatically, authorise suspension of concessions in circumstances where compliance has been achieved, it would necessarily act inconsistently with Article 22.5 of the DSU.²³

In this respect, the European Union recalls that the Appellate Body has found that the question of whether a measure found inconsistent with a covered agreement has been removed, as provided for in Article 22.8 of the DSU, necessitates a multilateral determination. Specifically, the Appellate Body has made the following findings:

Article 21.5 provides for specific procedures for adjudicating a disagreement as to the consistency with the covered agreements of measures taken by a Member to implement the DSB's recommendations and rulings. Thus, panel proceedings under Article 21.5 is the proper procedure for resolving the disagreement as to whether Directive 2003/74/EC has achieved substantive compliance and whether, consequently, the resolutive condition in Article 22.8 that requires the termination of the suspension of concessions has been met. ...²⁴

... Article 21.5 is cast in obligatory language. ...²⁵

In sum, we consider that recourse to Article 21.5 panel proceedings is the proper course of action within the procedural structure of the DSU in cases where, as in this dispute, a Member subject to the suspension of concessions has taken an implementing measure and a disagreement arises as to whether "the measure found to be inconsistent with a covered agreement has been removed" within the meaning of Article 22.8. Therefore, we share the European Communities' view that Article 21.5 panel proceedings are the procedures to be followed where there is disagreement as to whether Directive 2003/74/EC has achieved substantive compliance. ...²⁶

As the Appellate Body has explained, Article 23.1 lays down the fundamental obligation of WTO Members to have recourse to the rules and procedures of the DSU when seeking redress of a violation of the covered agreements. Article 23 restricts WTO Members' conduct in two respects. First, Article 23.1 establishes the WTO dispute settlement system as the exclusive forum for the resolution of such disputes and requires adherence to the rules of the DSU. Secondly, Article 23.2 prohibits certain unilateral action by a WTO Member. Thus, a Member cannot unilaterally: (i) determine that a violation has occurred, benefits have been nullified or impaired, or that the attainment of any objective of the covered agreements has been impeded;

²² Article 22.7 of the DSU provides as follows: "The arbitrator acting pursuant to paragraph 6 shall not examine the nature of the concessions or other obligations to be suspended but shall determine whether the level of such suspension is equivalent to the level of nullification or impairment. The arbitrator may also determine if the proposed suspension of concessions or other obligations is allowed under the covered agreement. However, if the matter referred to arbitration includes a claim that the principles and procedures set forth in paragraph 3 have not been followed, the arbitrator shall examine that claim. In the event the arbitrator determines that those principles and procedures have not been followed, the complaining party shall apply them consistent with paragraph 3. The parties shall accept the arbitrator's decision as final and the parties concerned shall not seek a second arbitration. The DSB shall be informed promptly of the decision of the arbitrator and shall upon request, grant authorization to suspend concessions or other obligations where the request is consistent with the decision of the arbitrator, unless the DSB decides by consensus to reject the request." (footnote omitted)

²³ Article 22.5 of the DSU provides as follows: "The DSB shall not authorize suspension of concessions or other obligations if a covered agreement prohibits such suspension."

²⁴ Appellate Body Report, *US-Continued Suspension*, para. 338.

²⁵ Appellate Body Report, *US-Continued Suspension*, para. 340.

²⁶ Appellate Body Report, *US-Continued Suspension*, para. 345.

(ii) determine the duration of the reasonable period of time for implementation; or (iii) decide to suspend concessions and determine the level thereof.²⁷ (footnote omitted)

... before obtaining the DSB's authorization to suspend concessions, a Member must initiate a dispute settlement process in which it challenges the consistency with the covered agreements of a measure taken by another Member. The Member initiating the process will only be authorized to suspend concessions when the measure is found by the panel (and the Appellate Body, if appealed) to be inconsistent with the covered agreements and the Member taking the measure fails to implement the panel's (or Appellate Body's) findings within a reasonable period of time or, if it takes a measure to comply, that measure is found by the panel (and the Appellate Body) in compliance proceedings not to have brought the Member concerned into compliance. In other words, the Member will only be able to suspend concessions pursuant to the DSB's authorization after having had extensive recourse to, and abided by, the rules and procedures of the DSU, consistent with the requirements of Article 23.1.²⁸

Accordingly, Indonesia's decision and request pursuant to Article 22.2 of the DSU, together with its omission in not initiating and pursuing compliance proceedings pursuant to Article 21.5 and its omission in not requesting and procuring suspension of the arbitration panel proceedings pending the outcome of the compliance panel proceedings, are inconsistent with that provision and with Articles 21.5, 23.1²⁹ and 23.2(a)³⁰ of the DSU because Indonesia has proceeded unilaterally, in circumstances in which there is a dispute with respect to compliance, without any multilateral determination of non-compliance.

In addition, Indonesia's request that the European Union be unlawfully excluded from the compliance/arbitration panel proceedings, which was a genuine and substantial cause of that exclusion, is inconsistent with: Article 10.1 of the DSU, because it does not ensure that the interests of other Members are fully taken into account; Article 10.2 of the DSU because the European Union has a substantial interest in the matter before the compliance/arbitration panel and has notified that interest to the DSB, but will not have an opportunity to be heard or to make written submissions; and Article 10.3 because the European Union has not received and will not receive all the submissions of the parties to the dispute to the first meeting.

* * * *

For the reasons stated, Indonesia's measures appear to nullify or impair benefits accruing to the European Union directly or indirectly under all of the above-cited agreements and provisions.

The European Union reserves the right to address additional measures and claims regarding the above matters in the course of the consultations.

The European Union looks forward to receiving Indonesia's reply in due course to this request for consultations. The European Union is ready to consider with Indonesia mutually convenient dates and modalities for organising the consultations.

²⁷ Appellate Body Report, *US-Continued Suspension*, para. 371.

²⁸ Appellate Body Report, *US-Continued Suspension*, para. 374.

²⁹ Article 23.1 of the DSU provides as follows: "When Members seek the redress of a violation of obligations or other nullification or impairment of benefits under the covered agreements or an impediment to the attainment of any objective of the covered agreements, they shall have recourse to, and abide by, the rules and procedures of this Understanding."

³⁰ Article 23.2(a) of the DSU provides as follows: "In such cases, Members shall:

(a) not make a determination to the effect that a violation has occurred, that benefits have been nullified or impaired or that the attainment of any objective of the covered agreements has been impeded, except through recourse to dispute settlement in accordance with the rules and procedures of this Understanding, and shall make any such determination consistent with the findings contained in the panel or Appellate Body report adopted by the DSB or an arbitration award rendered under this Understanding;"