

CHILE – TAXES ON ALCOHOLIC BEVERAGES

*Arbitration
under Article 21.3(c) of the
Understanding on Rules and Procedures
Governing the Settlement of Disputes*

Award of the Arbitrator
Florentino Feliciano

I. Reference to Arbitration

1. On 12 January 2000, the Dispute Settlement Body (the "DSB") adopted the Appellate Body Report¹ and the Panel Report², as modified by the Appellate Body Report, in *Chile - Taxes on Alcoholic Beverages* ("*Chile – Alcoholic Beverages*"). On 1 February 2000, Chile informed the DSB, pursuant to Article 21.3 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU"), that it would implement the recommendations and rulings of the DSB in this dispute but that it would require a "reasonable period of time" to do so, as provided for in Article 21.3 of the DSU.

2. Consultations between Chile and the European Communities regarding the duration of the reasonable period of time for implementation took place in Geneva, on 22 February 2000, and subsequently by telephone-conference, but these consultations did not produce agreement.

3. By joint letter of 27 March 2000, Chile and the European Communities notified the DSB that they had agreed that the duration of the reasonable period of time for implementation should be determined through binding arbitration, under the terms of Article 21.3(c) of the DSU, and that I should act as Arbitrator. The parties also indicated in that letter that they had agreed to extend the time-period for the arbitration process, fixed at 90 days by Article 21.3(c) of the DSU, by a further 51 days, that is until 31 May 2000. Notwithstanding this extension of the time-period for the arbitration process, the parties stated that the arbitration award would be deemed to be an award made under Article 21.3(c) of the DSU. My acceptance of this designation to act as Arbitrator was conveyed to the parties by letter of 28 March 2000.

4. Written submissions were received from Chile and the European Communities on 10 April 2000 and an oral hearing was held on 25 April 2000.

II. Arguments of the Parties

A. Chile

5. Chile begins its submission by noting that, under the *Constitución Política de la República de Chile* ("Constitution"), tax related matters must be regulated by formal laws (*leyes*) adopted by Chile's National Congress.³ The Constitution also upholds the "principle of tax legality" which

¹WT/DS87/AB/R, WT/DS110/AB/R.

²WT/DS87/R, WT/DS110/R.

³Articles 19 and 60, n° 2, of the Constitution; English translation in *Constitutions of the Countries of the World*, Blaustein and Flanz (eds.) (Oceana Publications, 1991), with supplement of 1997.

requires "the equal distribution of taxes, in proportion with individual income or in the progressive manner established by law."⁴ Implementation of the recommendations and rulings of the DSB can only be effected by the adoption of a law, by the National Congress, to amend the Additional Tax on Alcoholic Beverages (*Impuesto Adicional a las Bebidas Alcohólicas*) (the "ILA"). It is not possible for implementation to be carried out through the exercise of delegated powers by the executive department of the Chilean government.

6. Chile analyses in detail the legislative process that will be applicable to the enactment of a law to implement the recommendations and rulings of the DSB in this case.

7. The legislative process involves a "pre-legislative" stage which is not regulated by any constitutional or other legal text. This stage involves a technical, political and legal analysis of a proposed bill. An Inter-Ministerial Commission, comprising representatives of the Ministries of Finance, Economic Affairs, and Foreign Affairs, is currently examining the issues surrounding implementation and will submit a draft bill for consideration by the President of the Republic. Following a brief interruption, the work of the Commission continued after the national elections on 11 March 2000 and the change of government in Chile. The Commission's work could take a few more weeks.

8. The formal stages of the legislative process are: initiation, discussion, approval, endorsement, promulgation and publication. In tax matters, the exclusive power of initiative for a law lies with the President⁵, who must first propose the bill to the Chamber of Deputies of the National Congress.⁶

9. When a tax bill is proposed, it is sent, after certain preliminary formalities, to a standing committee of the Chamber of Deputies, in this case the Committee on Finance, for consideration of the general features of the bill.⁷ The Chamber of Deputies can, at its discretion, entrust consideration of the bill to more than one standing committee, to two or more standing committees jointly, or it can appoint special committees.⁸ The committees may approve or reject the bill or may introduce amendments to it.

10. The bill to amend the ILA could be examined by the following Committees: Finance (as it will influence fiscal revenues); Foreign Affairs (as it concerns compliance with an international

⁴Chile's submission, para. 7, citing Article 19, n° 20, of the Constitution.

⁵Article 62, n° 1, of the Constitution.

⁶Article 62 of the Constitution.

⁷Articles 17 and 21 of the *Ley Orgánica Constitucional del Congreso Nacional* (the "*Ley Orgánica*").

⁸Article 18 of the *Ley Orgánica*.

treaty); Agriculture (as it affects agricultural production); Economy (as it relates to the industrial sector), and Health (as it concerns the regulation of a product, alcohol, which affects public health).

11. The Committees report their conclusions to the Chamber of Deputies. The Chamber of Deputies then considers the general features of the bill and votes on whether to approve or reject the bill in principle. This is known as the "general discussion". If the bill is approved in principle, it is remitted to the Committee(s) for consideration, provision-by-provision, of its specific content. Following committee consideration, the Chamber of Deputies holds a "specific discussion" of the bill. The Chamber of Deputies may approve amendments to the text of the bill, and it may also send the bill back to the Committee(s) for further study and a second report.

12. If the bill is approved by the Chamber of Deputies, it is sent to the Senate, as the "Chamber of Review", which proceeds in the same manner as the Chamber of Deputies. If the bill is approved by both Chambers of the National Congress, it is sent to the President of the Republic for approval (or rejection). Should the President of the Republic not approve the bill, he returns it to the National Congress, with appropriate comments on it, within thirty days. The National Congress may then approve the comments or, by special majority, reject some or all of them. It may also reject the bill in its entirety. If approved, the bill is returned to the President of the Republic for promulgation.⁹

13. The President approves a bill, as the co-legislating authority, through an endorsement. However, if the President does not announce a decision of approval within 30 days, he is deemed to have approved the bill. The next stage is promulgation. A decree of promulgation, issued by the President, certifies the existence and the definitive text of the new law. Promulgation occurs within a time-period fixed by the Constitution.¹⁰

14. The decree of promulgation of the new law is sent for processing to the Office of the Comptroller General of the Republic, which records the law and registers the decree of promulgation. No deadline is set for this process. The act of registration by the Office of the Comptroller General involves a review of the legality and constitutionality of the decree of promulgation.

15. Publication adds the final touch to the law, bringing it into force. Publication must take place in the Official Journal within five working days following the processing of the decree of

⁹Article 70 of the Constitution.

¹⁰Articles 69, 70 and 72 of the Constitution.

promulgation. The date of the law is the date of its publication, without prejudice to the establishment in the same law of a different rule governing the date at which it is to enter into force.¹¹

16. "Urgency" is the mechanism by which the President of the Republic, as co-legislator, establishes the priorities of the National Congress' legislative agenda and speeds up the processing of a bill. Article 71 of the Constitution empowers the President to request that the National Congress pronounce itself upon a bill within a limited period of time. The detailed rules for the application of the urgency procedure are set forth in the *Ley Orgánica*. Under these provisions, three different urgency procedures are available. Under the simple urgency (*simple urgencia*) procedure, the Chamber of Congress concerned must debate and vote on the bill within a period of 30 days; under the extreme urgency (*suma urgencia*) procedure, the period is 10 days; and, under the immediate discussion (*discusión inmediata*) procedure, the period is 3 days.¹² The President determines, at his discretion, which of the three procedures to invoke. Urgency can be requested in any one or all of the stages of enactment. However, the Chamber of Deputies or the Senate may, and often do, reject the urgency period.

17. Chile notes that an examination of 38 relevant bills, on different subjects, approved by the National Congress in the past decade, shows a considerable divergence in the time required for enactment, ranging from three months to 97 months. The average duration for these bills was 33 months. Chile adds that, at any stage of the legislative process, a bill may be challenged before the Constitutional Court. During such a challenge, a bill cannot become law.

18. Having reviewed its national legislative procedure, Chile highlights certain "particular circumstances" of the case that it believes are relevant, under Article 21.3(c) of the DSU, in determining the reasonable period for implementation. First, Chile rejects the argument that "prompt compliance", as required under the DSU, means that an implementing Member must use an extraordinary procedure, such as the urgency procedure, in place of its usual legislative process. The reasonableness of the period of time cannot be fixed by taking account solely of the interests of the complaining party since the DSU is also intended to give the affected Member time to implement through the domestic legal channels by which implementation can objectively be effected.

19. Chile refers to the statement of the Arbitrator in *Korea – Taxes on Alcoholic Beverages* ("*Korea – Alcoholic Beverages*") that "although the reasonable period of time should be the shortest period possible within the legal system of the Member to implement the recommendations and rulings

¹¹Articles 7 and 8 of the Civil Code.

¹²Article 27 of the *Ley Orgánica*.

of the DSB, this does not require a Member, in my view, to utilise an *extraordinary* legislative procedure, rather than the *normal* legislative procedure ...".¹³ Moreover, Chile recalls that an implementing Member has a choice as to the means by which it chooses to implement.

20. Chile also observes that, under Article 21.2 of the DSU, "particular attention should be paid to matters affecting the interests of developing country Members...". This provision constitutes a mandate to "consider" the domestic reality of the developing country Member as a factor within the principle of prompt compliance. By seeking to exclude the political, economic and social consequences of implementation, the European Communities overlooks the relevance of Article 21.2. Chile, on the other hand, believes that account must be taken of the specific interests of the developing country Member in question.

21. To that end, Chile stresses the political sensitivity of the legal change that implementation in the present case requires. The new law will affect fiscal revenues, public health and the social and economic situation of pisco producers. Public opinion, and certain Members of Congress, consider that the pisco sector had already undergone significant adjustment when the ILA was enacted and find it difficult to understand why it should face further changes, particularly in view of pisco's great importance to the economy of the pisco producing regions. The implementing measure will probably also result in a decrease in the tax on whisky, which the public see as a luxury good and which does not generate direct employment in Chile. The implementation debate will also focus on the health effects of alcohol and its abuse, which is a problem in Chile. Any reduction in tax rates on alcohol will, therefore, be open to question.

22. These considerations reveal the complexity and the political sensitivity of the implementation process and indicate that a considerable period of time will have to be devoted to the legislative process. It is not a question of ensuring that the bill is given the most urgent possible legislative treatment. In view of this, Chile considers that the minimum reasonable period of time necessary to effect implementation is 18 months.

B. *European Communities*

23. The European Communities recalls that, under Article 21.3 of the DSU, a Member should comply immediately with the rulings and recommendations of the DSB. Under the same provision, it is only if this is impracticable that the Member concerned is granted a reasonable period of time for implementation. Under Article 21.3(c), 15 months is a "guideline" for the Arbitrator in determining

¹³Award of the Arbitrator under Article 21.3(c) of the DSU, *Korea – Alcoholic Beverages*, WT/DS75/16, WT/DS84/14, 4 June 1999, paragraph 42.

the duration of the reasonable period. It is not an entitlement. As clarified by the Arbitrator in *EC – Measures Concerning Meat and Meat Products (Hormones)* ("*European Communities – Hormones*")¹⁴, and reiterated in *Indonesia – Certain Measures Affecting the Automobile Industry* ("*Indonesia – Automobile Industry*")¹⁵, in *Australia – Measures Affecting Importation of Salmon* ("*Australia – Salmon*")¹⁶, and in *Korea – Alcoholic Beverages*¹⁷, "the reasonable period of time should be the *shortest period possible within the legal system of the Member to implement the recommendations and rulings of the DSB.*" (emphasis added)

24. In determining what is "reasonably practicable", the Arbitrator should consider exclusively:

- the nature of the required implementing measures (for instance, whether legislative or merely administrative measures are needed);
- the procedures which must be followed for adoption of that type of measure under the domestic law of the Member concerned; and
- the degree of complexity of the measures to be adopted, resulting in particular from the content of those measures.

25. The political, economic or social consequences of the implementing measures are not, as such, pertinent factors which the Arbitrator may take into account in fixing the duration of the reasonable period. As the Arbitrator in *Indonesia – Automobile Industry* said, the need for an industry to make structural adjustments in order to be able to meet competition from imports is not a "particular circumstance" to be taken into account, under Article 21.3(c), in determining the duration of the reasonable period of time.¹⁸

26. The European Communities observes that the measure at issue in *Chile – Alcoholic Beverages*, the ILA, is a law adopted by Chile's National Congress.¹⁹ Chile has indicated that

¹⁴Award of the Arbitrator under Article 21.3(c) of the DSU, WT/DS26/15, WT/DS48/13, 29 May 1998, para. 26.

¹⁵Award of the Arbitrator under Article 21.3(c) of the DSU, WT/DS54/15, WT/DS55/14, WT/DS59/13, WT/DS64/12, 7 December 1998, para. 22.

¹⁶Award of the Arbitrator under Article 21.3(c) of the DSU, WT/DS18/9, 23 February 1999, para. 38.

¹⁷*Supra*, footnote 13, paras. 36-37.

¹⁸*Supra*, footnote 15, para. 23.

¹⁹The original ILA was introduced through Decree-Law No. 825/1974. The ILA was amended by in 1997 by Law No. 19,534. It was this amended system of taxation which is the subject of the DSB's recommendations and rulings in *Chile – Alcoholic Beverages*.

implementation of the DSB's recommendations and rulings in this case will require that law to be amended, which, in turn, will entail the enactment of a new law by the National Congress.

27. The European Communities summarises the Chilean legislative process, reiterating much of what Chile stated. It also recalls that the National Congress meets in ordinary session between 21 May and 18 September. The European Communities notes that, besides its ordinary sessions, the National Congress may be convoked to meet in extraordinary session, at the request of the President of the Republic or on its own motion.²⁰ The European Communities suggests that extraordinary sessions are convened "regularly" in Chile.²¹

28. The European Communities submits that, in practice, completion of the legislative process, from the moment that a bill is sent by the President of the Republic to the National Congress, takes, as a general rule, 2 to 5 months.

29. The European Communities also adds that laws on any subject-matter may be adopted within a much shorter period of time in case of urgency, using the special urgency procedures outlined in the Constitution and *Ley Orgánica*. It contends that, using the urgency procedures, a bill may be adopted within one month or less. According to the European Communities, the urgent procedure has been used "regularly" for tax legislation in Chile.²²

30. The European Communities argues that previous legislative amendments, including to tax legislation, have often taken no more than a few months to be approved, and have taken effect immediately. For instance, according to the European Communities, under the non-urgent procedure, enactment of Law No. 19,633/1999, which effected a decrease in the taxation on luxury cars, required only two and a half months. Another example is provided by Law No. 19,642/1999, on the granting of the status of "exporter" to enterprises exploiting public use harbours, which required four and a half months.

31. Even the most recent amendment of the ILA itself, which resulted in the measure at issue in *Chile – Alcoholic Beverages*, did not take more than six months from proposal by the President to promulgation; and it entered into force only one month later. The European Communities emphasizes that this amendment involved the introduction of an entirely new system of taxation for distilled spirits and required careful consideration and explanation of its economic impact.

²⁰Article 52 of the Constitution.

²¹European Communities' submission, para. 23.

²²European Communities' submission, para. 29.

32. Against this background, the European Communities submits that the implementation process in the present dispute can be completed in a "few months" and, thus, in a period of time "much less" than the period Chile seeks.²³ The necessary legislation could be introduced into the National Congress at an extraordinary session of the Congress. However, even if the next ordinary session of the National Congress, on "18 May 2000", were awaited, the new law could still be promulgated by the close of that session on "21 September 2000".²⁴ This is only 8 months from the date of adoption. The European Communities notes, additionally, that the "shortest period possible within the legal system" of Chile would involve the use of the urgency procedures, as has been done for other tax-related laws.

33. The European Communities suggests that the contemplated form of implementation, outlined in consultations with Chile, will probably maintain the existing *ad valorem* basis of taxation. The amendment will, therefore, be essentially technical and will not require "any substantial time."²⁵

34. For these reasons, the European Communities requests the Arbitrator to rule that the reasonable period of time for Chile to implement the recommendations and rulings of the DSB be, at most, 8 months and 9 days²⁶ from the date of adoption of the Appellate Body and Panel reports by the DSB.

III. Reasonable Period of Time

35. The sole issue to be resolved in this arbitration is this: what is "the reasonable period of time", within the meaning of Article 21.3 of the DSU, for implementation of the recommendations and rulings of the DSB in *Chile – Alcoholic Beverages*.

36. It is not disputed by either of the parties to this arbitration that "implementation" in *Chile – Alcoholic Beverages* involves the modification of the ILA to render it consistent with Article III:2 of the *General Agreement on Tariffs and Trade 1994* (the "GATT 1994"). An amendatory law enacted by the National Congress of Chile is necessary, given the requirements of the Constitution and laws of Chile; the required modification cannot be effected by an executive or administrative issuance. The issue to be resolved thus translates into what is "the reasonable period of time" for enacting and putting into legal effect an amendatory law that would render the existing ILA consistent with the GATT 1994.

²³European Communities' submission, para. 43.

²⁴*Ibid.*, paras. 44 and 45.

²⁵*Ibid.*, para. 47.

²⁶At the oral hearing on 25 April 2000, the European Communities stated it would concede another 9 days to Chile, that is, the reasonable period should expire on 30 September 2000.

A. *General Considerations*

37. It is always salutary to recall the basic injunction of Article 21.1 of the DSU, that "*prompt compliance*" with the DSB recommendations and rulings is "essential" for the "effective resolution of disputes to the benefit of all Members." Two paragraphs later, in Article 21.3, the DSU recognizes that to require the Member concerned "to *comply immediately*" with the DSB recommendations and rulings may, in some situations, be "*impracticable*". In such situations, the Member concerned "shall have a reasonable period of time to do so."

38. The DSU clearly stressed the systemic interest of all WTO Members in the Member concerned complying "immediately" with the recommendations and rulings of the DSB. Reading Articles 21.1 and 21.3 together, "prompt" compliance is, in principle, "immediate" compliance. At the same time, however, should "immediate" compliance be "impracticable" – it may be noted that the DSU does not use the far more rigorous term "impossible" – the Member concerned becomes entitled to a "reasonable period of time" to bring itself into a state of conformity with its WTO obligations. Clearly, a certain element of flexibility in respect of time is built into the notion of compliance with the recommendations and rulings of the DSB. That element would appear to be essential if "prompt" compliance, in a world of sovereign states, is to be a balanced conception and objective.

39. The concept of reasonableness, which is, of course, built into the notion of "a reasonable period of time" for implementation, inherently involves taking into account the relevant circumstances. In some cases these circumstances may be singular or few in number but in other cases they may be multiple. Determination of a "reasonable period of time" is not, in principle, appropriately carried out by ascribing decisive or exclusive relevance to one single or even a few *a priori* factors and eschewing consideration of everything else as non-pertinent. Thus, the shortest period of time *theoretically* possible for the completion of the legislative process, even assuming the bill enjoys the necessary parliamentary majority from the beginning and is never the subject of serious debate, is not the *sole* criterion that I should take into account in determining the reasonable period. What Article 21.3(c) of the DSU provides arbitrators with is a "*guideline*", not a fixed command, that the reasonable period should be not more than 15 months from the date of adoption by the DSB of the pertinent Panel and Appellate Body Reports. Article 21.3(c) evidently contemplates a case-specific approach and authorizes the consideration of the "particular circumstances" of a given case, which may warrant a longer or shorter period.

40. In assessing the duration of the reasonable period, the provisions of Article 22 of the DSU are also noteworthy. Under Article 22.1, although "a reasonable period of time" may have elapsed without compliance with the recommendations and rulings of the DSB, *neither* compensation

nor suspension of concessions or other obligations is to be "preferred to full implementation", by bringing the measure concerned into conformity with WTO obligations. Thus, in fixing the reasonable period, I should take account of the fact that full and effective implementation is "preferred".

B. *Particular Circumstances*

41. I turn to consideration of "particular circumstances" which one or the other party has submitted are pertinent in assessing a "reasonable period of time" to comply with the recommendations and rulings of the DSB. Since compliance here means *adoption of a law* appropriately amending the ILA, the reference here is to circumstances which rationally bear upon the time necessary for *enactment* of such a law. In its written submission, the European Communities had argued that Chile was not entitled to build into the notion of reasonable time to comply the time needed for structural adjustment of Chile's pisco producing industry. At the oral hearing, Chile clarified that it was *not* asking for time for its pisco industry to adjust to the requirements of a WTO-consistent tax system before enacting the necessary amendatory law. Thus, it is not necessary to deal any further with the European Communities' argument except to note that the time a domestic industry may need to adapt itself to new tax rates does not, in itself, relate to the time needed or appropriate *for the enactment of the necessary amendatory law* in this case.

42. In submitting that 8 months and 9 days from 12 January 2000 is a "reasonable period of time" for Chile to implement the recommendations and rulings of the DSB, the European Communities contends that the amendatory bill could well be introduced by the President of Chile upon calling an extraordinary session of the National Congress specifically to act upon that and possibly other bills. The European Communities also suggests that the urgency procedures available under the Constitution could be used by the President. It is my belief, however, that the Member concerned, has the sovereign prerogative and responsibility of determining for itself the most appropriate, and probably effective, method of implementing the recommendations and rulings of the DSB by securing the passage of the amendatory law. The choice and the timing of the detailed operating steps in enacting a new law are properly left to the Member concerned. Chile will be concerned with bringing about the *successful* enactment of the law that would modify the existing ILA, given the objective structures, constitutional norms and practices which effectively constitute the multi-phased legislative process in Chile.

43. Two aspects of the Chilean legislative process may be usefully noted. One is the set of practices designated as the "pre-legislative" phase of the law-making process in Chile, during which phase a specific revised tax scheme is developed and proposed on the basis of consultations and

technical assessments. These consultations will include discussions aimed at building and organizing the broad support necessary for the adoption of the proposed bill, by both Chambers of the National Congress. The duration of this "pre-legislative" phase may differ from bill to bill; no maximum period is set by law but it is clearly an important phase if the success of the legislative effort is important. The other aspect is the lack of constitutionally fixed time frames for initiating and completing each stage of the legislative process, *prior to* the time the bill is sent to the President (as the co-legislating authority) for his approval and promulgation. Only presidential approval (or disapproval) and promulgation of the approved law are subject to prescribed maximum time periods under the Constitution.

44. Chile has also referred to Article 21.2, where the DSU, immediately after stressing that "prompt compliance" with the recommendations and rulings of the DSB is essential for the WTO dispute settlement system, provides:

Particular attention should be paid to matters affecting the interests of developing country Members with respect to measures which have been subject to dispute settlement.

Chile has submitted that account must be taken of the specific interests of Chile as the developing country Member whose measure has been the subject of dispute settlement. However, Chile has not been very specific or concrete about its particular interests as a developing country Member nor about how those interests would actually bear upon the length of "the reasonable period of time" to enact necessary amendatory legislation.

45. It is not necessary to assume that the operation of Article 21.2 will essentially result in the application of "criteria" for the determination of "the reasonable period of time" – understood as the *kinds* of considerations that may be taken into account – that would be "qualitatively" different for developed and for developing country Members. I do not believe Chile is making such an assumption. Nevertheless, although cast in quite general terms, because Article 21.2 is in the DSU, it is not simply to be disregarded. As I read it, Article 21.2, whatever else it may signify, usefully enjoins, *inter alia*, an arbitrator functioning under Article 21.3(c) to be generally mindful of the great difficulties that a developing country Member may, in a particular case, face as it proceeds to implement the recommendations and rulings of the DSB.

IV. The Award

46. Having regard to, *inter alia*, the written and oral submissions of both parties, the general and more particular considerations indicated above, and the circumstances constituting this case, it is my

determination that the reasonable period of time for Chile to implement the recommendations and rulings adopted by the DSB in *Chile – Alcoholic Beverages* by enacting and putting into effect a law appropriately amending its ILA, is not more than 14 months and 9 days from 12 January 2000, that is to say, until 21 March 2001.

Signed in the original at Geneva this 19th day of May 2000 by:

Florentino Feliciano
Arbitrator