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Chris Brown

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CHINA’S GATT BID:
WHY ALL THE FUSS ABOUT CURRENCY CONTROLS?

Chris Brown

Abstract: China did not succeed in its bid to join the General Agreement on Tariffs and Trade (GATT) during the Uruguay Round. A key stumbling block was China’s mechanism of exchange rate controls. From the mid-1980s to the end of 1993, China used a dual-rate currency mechanism, administering these rates through a loose network of about 100 exchange centers ("swap centers"). The swap centers helped to create partial convertibility of the Chinese currency and were instrumental in creating incentives for China’s exporters and in attracting foreign investment. However, the swap centers also caused trade conflicts with the U.S. and within GATT. China was accused of using its dual rates to subsidize its state sector, and of using the swap centers as a means to block imports by limiting access to foreign exchange. Meeting privately, the GATT working party was no doubt concerned that GATT and IMF rules would be inadequate to police China’s exchange rate policies if China was admitted to GATT. Not surprisingly, the working party decided to reject China’s bid. In 1994, China unified its dual-rate regime and established an inter-bank market for foreign exchange. While China continues to seek a seat within GATT’s successor, the World Trade Organization, it is still far from clear whether China has established a currency mechanism that comports with GATT principles. In particular, there are legitimate concerns about the transparency of the new inter-bank market and the extent to which China will continue to use currency measures to hinder imports.

“I don’t want to belong to any club that will accept me as a member.”
—Groucho Marx

I. INTRODUCTION

Among the few international organizations in which China cannot claim membership is the General Agreement on Tariffs and Trade (GATT), the Geneva-based body in charge of global trade matters. China joined the International Monetary Fund (IMF) and the World Bank in 1980, but it remains an observer to GATT. During the seven-year Uruguay Round of

1 JOHN BARTLETT, FAMILIAR QUOTATIONS 834 (1980).
3 The Republic of China was one of the founding members of the original GATT charter on October 30, 1947, but Chiang Kai-shek’s government withdrew from GATT in March of 1950, following Mao Tse-dong’s takeover of mainland China and the establishment of the People’s Republic of China (PRC) on the
Multilateral Trade Talks, which ended on December 15, 1993, Beijing made a concerted effort to join GATT but did not succeed. Following the Uruguay Round, China continues to pursue GATT membership, and some GATT members voice support, but China remains on the outside. It remains an open question what role China will play in the successor to GATT, the World Trade Organization, which is expected to be established in 1995.


4 The Uruguay Round of multilateral trade talks began in Punta del Este, Uruguay, in November 1986, and ended in Geneva, Switzerland, on December 15, 1993. See *generally Uruguay Round Agreement is Reached; Clinton Notifies Congress Under Fast Track; Negotiators Clear Path to GATT Pact by Sweeping Away Remaining Differences*, 10 INT'L TRADE REP. (BNA) 2103 (Dec. 15, 1993) [hereinafter *Uruguay Round Agreement is Reached*].

5 To demonstrate Beijing's resolve to the GATT working party, China announced a number of reforms during the Uruguay Round. Although some of these announcements were cosmetic, as a whole they reflected China's desire to show that it was making progress towards meeting GATT's concerns. See, e.g., *China Approves Changes in Constitution, Government to Reflect Market Economy Shift*, 10 INT'L TRADE REP. (BNA) 549 (Mar. 31, 1993) [hereinafter *China Approves Changes in Constitution*] (China enacted constitutional changes in 1993 under which the state's role in the economy was theoretically reduced. China's constitution was revised to show that the state "strengthens economic legislation [and] improves macroeconomic regulations." The earlier constitution stated that the government was responsible for "overall balancing by economic planning."); *Chinese Trade Official Outlines Proposed GATT-Compatible Trade Reforms*, 9 INT'L TRADE REP. (BNA) 387 (Mar. 4, 1992) (describing elimination of import licenses for 16 product categories); *China's Legislature Approves Membership in Two Copyright Protection Conventions*, 9 INT'L TRADE REP. (BNA) 1177 (July 8, 1992) (reporting China's decision to join the Berne Convention for the Protection of Literary and Artistic Works and the World Copyright Convention); *China Announces Tariff Cuts on Over 3,000 Types of Commodities*, 9 INT'L TRADE REP. (BNA) 2185 (Dec. 23, 1992).


8 The World Trade Organization is intended to replace GATT in January 1995. GATT set up a committee to lay the groundwork for the WTO in March 1994. Among this committee's tasks is to decide which countries that are currently in the process of applying to GATT (such as China) will be allowed into the WTO. *Delegates Set Up Committee to Study Establishment of WTO*, 11 INT'L TRADE REP. (BNA) 462 (Mar. 23, 1994) [hereinafter *Delegates Set Up Committee*].
The fundamental difficulty for China has been trying to integrate its largely non-market economy with the market-based principles of GATT. With 116 member nations, GATT is based on the general principle that trade levels can be increased (and trade wars avoided) through multilateral tariff reductions and nondiscriminatory treatment among all members. In market economies, tariff cuts are presumed to have a direct effect on prices, and thereby have an influence on the decisions of consumers and the incentive structure of industry. In non-market economies such as China, the effects of tariff cuts are more difficult to gauge. Not surprisingly, China's negotiations with GATT have dealt with tariffs as only one issue among several others. Additionally, GATT members (particularly the United

9 It is risky to label China's economy as "planned" given the increasing amount of private economic activity, but clearly central planning continues to play an important role in China's political economy. See generally CHINA: REFORM AND THE ROLE OF THE PLAN IN THE 1990S, World Bank Country Study (1992) [hereinafter WORLD BANK COUNTRY STUDY]. In 1991, China began to characterize itself as a "socialist market economy" rather than a "socialist commodity economy," but Chinese leaders did not define the difference. China's claims to be a "market economy" were one of the issues that bogged down the GATT talks. See James McGregor, China's Failure to Define Its Economy Stalls GATT Entry. Says U.S. Envoy, ASIAN WALL ST. J., Mar. 8, 1993, at A4 [hereinafter China's Failure to Define its Economy].

10 There were 116 GATT members as of the close of the Uruguay Round on December 15, 1993. Uruguay Round Agreement is Reached, supra note 4, at 2103.

11 A nation's commitments under GATT can be roughly divided into tariff concessions and the general Most-Favored-Nation provision. Article II, Schedule of Concessions, explains the responsibilities of all GATT members as to tariff reductions. The operative language is the following: "Each contracting party shall accord to the commerce of the other contracting parties treatment no less favorable than that provided for [in the attached tariff reduction schedule]." (Emphasis added). The GATT charter originally contained a schedule of tariff cuts agreed to by all contracting parties. GATT CHARTER art. 11, 1(a).

Article I of GATT, General Most-Favoured-Nation Treatment, explains the general GATT principle that members must not discriminate among members, whether in the form of tariffs or other means:

With respect to customs duties and charges of any kind imposed on or in connection with importation or exportation or imposed on the international transfer of payments for imports or exports, and with respect to the method of levying formalities in connection with importation and exportation, . . . any advantage, favour, privilege or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other contracting parties.

GATT CHARTER art. I, ¶ 1. Although in modern times GATT has provided a forum to discuss trade disputes and to monitor adverse trade practices, the initial purpose of the organization was to bring about multilateral tariff reductions in the post-World War II reconstruction era. See U.S. DEP'T OF STATE, COMMERCIAL POLICY SERIES, PUB. NO. 2983, ANALYSIS OF GENERAL AGREEMENT ON TARIFFS AND TRADE 109 (Nov. 1947).

12 See GATT CHARTER art. I, ¶ 1.

13 JACOBSON & OKSENBERG, supra note 2, at 89.

14 China's initial bargaining position was that reducing tariffs alone would be the best way to increase imports. In 1986, China had considerable leeway to cut import tariffs, which averaged 44%. JACOBSON & OKSENBERG, supra note 2, at 90 & n.12.
States, the European Community members, and Japan) have focused on China's non-tariff barriers to trade, such as state planning, subsidies, price controls, and state-run industry. The difference between the Chinese delegation and the GATT members could be summed up as follows: for GATT, the question is how to absorb China without diluting its commitment to market-based trade. For China, the issue is how to join GATT without giving up the necessity of state ownership and some degree of centralized planning.

This Comment focuses on one of the key obstacles for China in its bid to join GATT: China's dual-rate currency regime. Normally, currency issues command little attention within GATT, but China's bid during the Uruguay Round presented a unique situation because China's restrictions on foreign exchange had long been a vital element in its trade reforms. Ironically, China's oft-criticized exchange rate regime was one of the key reasons for its foreign trade success. The Uruguay Round provided a unique opportunity in that it directed international scrutiny towards China's currency mechanism and ultimately encouraged China to overhaul this mechanism as a precondition for GATT entry.

Part II of this Comment presents an overview of China's dual-rate currency mechanism from the early 1980s up to the end of 1993, and the main criticisms of this system by China's trading partners, especially the

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15 In the first four years of the Uruguay Round, talks between the GATT working group and China focused on gathering information on China's trade and economic reforms. See generally GATT Rejects New Chinese Membership Bid, Requests More Data on Trade Liberalization, 7 INT'L TRADE REP. (BNA) 1477 (Sept. 26, 1990) [hereinafter GATT Rejects]. The amount of information requested was staggering: By mid-1988, GATT members had put forth over 1,200 questions regarding China's economic structure, a record number. JACOBSON & OKSENBERG, supra note 2, at 96.

16 China's deemed importance as an upcoming trading power is often cited as justification for including China within GATT. JACOBSON & OKSENBERG, supra note 2, at 88-9. But it has also been noted that China generally needs GATT more than GATT needs China, as demonstrated by China's efforts to change its domestic policies to conform with GATT principles. Chiu, supra note 3, at 8-10.

17 Former Chinese leader Zhao Ziyang told a visiting GATT delegation in 1986, that he believed China's planned commodity economy, the intended outcome of China's reforms, would accord with GATT's market-oriented principles and be sufficient for China's entry. JACOBSON & OKSENBERG, supra note 2, at 92. China's economy has changed significantly since 1986, but Chinese leaders have continued to uphold the need for an active state role in economic activity, despite GATT's focus on market economic principles. For example, China altered its constitution in 1993, but the change was minor. Under the new constitution, the government oversees "state-owned enterprise," rather than "state-run enterprise" as it did prior to the 1993 revision. See China Approves Changes in Constitution, supra note 5, at 549. China claimed to be a "market economy" near the close of the GATT talks, but this contention was itself a stumbling block between China and GATT. See China's Failure to Define its Economy, supra note 9, at A4.

U.S. Part III examines how the GATT charter and the Articles of Agreement of the IMF handle exchange rate issues, and why the GATT-IMF legal framework is not capable of policing exchange rate systems that are used to further trade goals. Finally, Part IV examines China's January 1994, currency reforms, and considers whether they will facilitate China's entry to GATT. If China is eventually admitted to GATT, a related issue considered herein is what conditions could be attached to China's protocol of accession in order to shield international trade from adverse currency measures.

II. CHINA'S CURRENCY PRACTICES

A. Overview: The Difference Between Import Controls v. Currency Restrictions

Imagine a developing nation that wants to restrict the import of sports cars. It might choose between two general routes. First, it could enact a heavy import tariff, quota, or even an outright ban to make it more costly to import foreign cars and more favorable to buy locally-built cars. This would be a trade measure used to restrict imports. Or, to achieve the same ends, the nation’s central bank could simply refuse to allocate hard currency for the purchase of imported cars.19 The second choice is actually a monetary restriction that in effect restricts imports. Roughly speaking, it is the latter choice that has been used in China in the mid-1980s20 and early 1990s.21 China has shown that managing access to foreign currency is an effective way to restrict unwanted imports.22

Historically, China has been able to restrict trade flows through currency measures because it has enforced various degrees of control23 on the

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19 This analogy is commonly used to point out the link between currency measures and trade. See Frieder Roessler, The Relationship Between the World Trade Order and the International Monetary System, in 5 THE NEW GATT ROUND OF MULTILATERAL TRADE NEGOTIATIONS: LEGAL AND ECONOMIC PROBLEMS 363, 375-76 (Ernst-Ulrich Petersmann & Menihard Hilf eds., 1988) [hereinafter The Relationship].
20 LARDY, supra note 18, at 59.
22 See generally LARDY, supra note 18, at 59; China Removes Controls, supra note 21, at 26.
23 China had very strict, centralized control over foreign exchange from 1950 to 1979. LARDY, supra note 18, at 27, 51. In 1979, the central government took the first steps to relinquish its monopoly on the retention of foreign currency, but the government continued to exercise control over access to hard currency bank accounts. Id. at 52.
conversion of its currency unit, the yuan, into other hard currencies. Throughout the world, foreign trade generally is conducted with the U.S. dollar, the Japanese yen, or the German mark, along with a few other convertible currencies. Many newly industrialized nations such as South Korea, Taiwan, and Thailand have liberalized their currency regulations to allow for convertibility, subject to various restrictions on account holding and repatriation of funds. Unlike these newly-industrialized countries, which often have large monetary reserves and relatively stable inflation, developing nations like China, India, and the Philippines generally face a more volatile economic situation in terms of monetary reserves, inflation, and unemployment. Thus, these nations tend to enforce very strict rules on the use of foreign exchange. Typically, a develop-

24 China's currency is the renminbi ("the people's money"), measured in units called yuan.
25 South Korea places restrictions on the amount of foreign currency that domestic firms, trading companies, institutional investors, and insurance companies can hold in bank deposits. Residents can have domestic foreign currency accounts, but individuals are not permitted to have offshore foreign currency accounts. Restrictions also apply to the amount of foreign currency that South Korean travelers can take out of the country. See FINANCING FOREIGN OPERATIONS, SOUTH KOREA 6-10 (Economist Intelligence Unit, May 1993).
26 Taiwan removed most of its foreign exchange regulations in mid-1987. All trade-related foreign exchange transactions are unrestricted, but the central bank restricts the amount that residents can remit in or out of Taiwan for those remittances that involve a conversion into or out of New Taiwan dollars. See FINANCING FOREIGN OPERATIONS, TAIWAN 10 (Economist Intelligence Unit, Nov. 1993).
28 Nation International Reserves (billion US$) Consumer Price Change (% change 8/93-8/94)
Taiwan $87.26 (Apr. 94) +3.4
Singapore $50.67 (Mar. 94) +3.2
South Korea $20.98 (Apr. 94) +6.0
Thailand $26.55 (May 94) +5.4
Source: Prices & Trends, FAR EASTERN ECON. REV., Aug. 11, 1994, at 72-73.
29 Nation International Reserves (billion US$) Consumer Price Change (% change 8/93-8/94)
China $29.83 (Mar. 94) +21.3
India $15.83 (May 94) +6.1
Philippines $6.03 (Apr. 94) +9.9
Source: Prices & Trends, FAR EASTERN ECON. REV., Aug. 11, 1994, at 72-73.
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An opining nation will require people seeking to convert local money into hard currency to state \textit{why} they need the hard currency. In this way, the state can turn down people who want to "raid" the state bank account in order to pay for imported goods that are not deemed necessary by the state.

China's policy of controlling trade flows through currency measures has raised difficult questions for trade policy makers, especially in the U.S. As China has liberalized its trade sector and pursued a place within \textit{GATT},\textsuperscript{32} the U.S. has benefited by increasing its exports to China.\textsuperscript{33} However, China's phenomenal trade growth,\textsuperscript{34} its trade deficits with the U.S.,\textsuperscript{35} and its bid to join \textit{GATT} have excited a renewed interest in the link between currency controls and free trade principles. The U.S. Department of the Treasury has led this charge, citing China for manipulating its currency in three consecutive semi-annual reports to Congress.\textsuperscript{36} The U.S. Commerce Department and its International Trade Commission has also scrutinized the effects of China's currency controls in dumping disputes.\textsuperscript{37}

\textsuperscript{32} See supra note 5.

\textsuperscript{33} U.S. exports to China were forecast to reach US$ 8.2 billion in 1993, an increase of 10.6% over 1992. Imports from China were expected to reach US$ 29.5 billion, up 14.6%. Search of National Trade Databank, U.S. Foreign Trade Update-Monthly, Int'l Trade Admin., year-end 1993.

\textsuperscript{34} China's merchandise exports stood at US$ 25.7 billion in 1986, the start of the Uruguay Round, and had more than doubled to US$ 51.5 billion by the end of 1990. From 1991 to 1993, merchandise exports continued to increase. At the end of 1991, exports were US$ 58.9 billion, and had grown to US$ 69.6 billion by the end of 1992. 1993 IMF \textit{Int'l Fin. Stat.} Y.B. 281. By the end of 1993, they were forecast to reach US$ 72.8 billion. \textit{China Country Report 9} (Economist Intelligence Unit, 4th Qtr. 1993).


\textsuperscript{36} § 3004 and § 3005 of the Omnibus Trade and Competitiveness Act of 1988, requires the U.S. Treasury to present to Congress semi-annual reports on international monetary and exchange rate policy. See DEPARTMENT OF TREASURY, REP. TO CONGRESS ON INT'L ECONOMIC AND EXCHANGE RATE POL'Y I (Nov. 1993) [hereinafter NOV. 1993 TREASURY REP.].

In the November 1993 report, Treasury for the third consecutive time concluded that China was manipulating its currency within the meaning of § 3004, and thereby gained an unfair competitive advantage. \textit{Id.} at 26. Treasury first leveled this charge of exchange rate manipulation in its December, 1992 report. DEPARTMENT OF TREASURY, REP. TO CONGRESS ON INT'L ECONOMIC AND EXCHANGE RATE POL'Y 34 (Dec. 1992) [hereinafter DEC. 1992 TREASURY REP.]. Treasury made the same charge in its May 1993 report. DEPARTMENT OF TREASURY, REP. TO CONGRESS ON INT'L ECONOMIC AND EXCHANGE RATE POL'Y 26 (May 1993).

\textsuperscript{37} In 1988, the International Trade Administration investigated complaints that caps, hats, and visors from China were being dumped in the U.S. at less than fair market value. Among the ITA's conclusions was that China was a "state-controlled economy" within the meaning of § 773(a) of the \textit{Tariff Act of 1930}. The ITA based this conclusion in part upon Chinese government control over currency quota allocation, foreign exchange earning targets, and limited convertibility of the currency. Final Determination of Sales at Less Than Fair Value; Certain Headwear From the People's Republic of China, 54 Fed. Reg. 11983, 11985 (Int'l Trade Admin. 1989).
In addition, China's currency regime has become a hot topic within GATT. Since 1986, when China first put forth its bid to re-join the organization, the GATT working party assigned to China's application has discussed a range of China's economic reforms. As an applicant, China was required to submit detailed reports on its economic and trade structure, and answer questions from the working party. Initially, the talks dealt with issues such as price reform, state subsidies, the publication of rules, and import licensing. In the last three years, however, currency controls became a focus of China's GATT talks. So central had the monetary issue become by the end of the Uruguay Round that China finally agreed with the working party that currency reform would be necessary to join GATT. How the parties came to hold this viewpoint presents an interesting study of global trade law and diplomacy.

B. China's Currency Situation Prior to the mid-1980s

Up to about the mid-1980s, China's currency unit, the yuan, was sheltered from the outside world. Most of the country's economy had no access to foreign currency and operated exclusively by using the yuan. Trade was centralized in about 15 state-run trading enterprises, and China's main exports were limited to commodities and a few light industrial goods. China's trade structure was only just beginning to resemble that of Taiwan and Hong Kong, with their emphasis on exports of industrial and manufactured goods.

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38 See JACOBSON & OKSENBERG, supra note 2, at 96.
39 The working party first met to discuss China's bid on February 23, 1988. Press reports indicate that the group focused on a range of issues, including quotas, subsidies, state trading organizations, and transparency in trade negotiations. GATT Working Group on P.R.C. Membership Bid Meets, But Decision Expected to Take Years 5, INT'L TRADE REP. (BNA) 253 (Feb. 24, 1988) [hereinafter GATT Working Group].
42 See WORLD BANK COUNTRY STUDY, supra note 9, at 48.
43 From 1980 to 1985, China's main export category was mineral-based fuels, food products, and non-food products such as oil seeds, textile fibers, and animal and vegetable raw materials. Manufactured goods were skewed towards textiles and fabrics. Export of metal-based manufactured products and machinery were stagnant. See WORLD BANK COUNTRY STUDY, supra note 9, at 204.
44 From 1982 to 1992, over 92% of Taiwan's annual exports have been industrial goods. During this period, Taiwan's overall exports grew from US$22.20 billion to US$61.47 billion. DIRECTORATE-GENERAL OF BUDGET, ACCOUNTING AND STATISTICS, 1993 STAT. Y.B. REPUBLIC OF CHINA 248.
In the 1980s, China began to open its trade sector to the global economy, but several decades of economic isolation meant that China faced considerable monetary risks. In the 1950s and 1960s, Beijing had followed a policy of strict import substitution, where the goal of foreign trade had been to achieve self-sufficiency. Imports were heavily skewed towards production equipment, while exports were viewed as wasteful. One result of this focus on self-sufficiency was that the exchange rate of the yuan was overvalued and many strategic imports (such as steel, machinery, and equipment) were subsidized out of the state's foreign currency reserves. Thus, China's central bank, the People's Bank of China (PBC), had total control over foreign exchange in China. It would allocate hard currency to import certain necessary machinery, and this machinery would in turn be sold at artificially low yuan-denominated prices to domestic factories. In effect, the Bank of China would absorb a currency loss on these transactions. Starting in 1964, China lessened such currency losses by setting up a separate, devalued rate of the yuan which was used to price certain imports. This raised some prices on imported goods closer to their world prices, and helped to stem the central bank's losses on imports.

China's overvalued currency produced more intractable losses on exports. In the 1950s and 1960s, China experienced the same problem.

From 1980 to 1990, Hong Kong's principal export categories were apparel and clothing accessories, watches and clocks, electrical machinery, textiles, electronic components, and jewelry. These six categories accounted for about 60% of total domestic exports. HONG KONG CENSUS AND STATISTICS DEPARTMENT, HONG KONG SOCIAL AND ECONOMIC TRENDS: 1980-1990 at 46 (1991).

45 China began to promote export processing in 1979. Imported components and raw materials were ear-marked for export producing firms, and the state began to ensure that these firms received a steady supply of domestic inputs such as electricity, fuel, and raw materials. Two other key steps in export development were the passage of the joint-venture law in 1979, and the establishment of the first special economic zones on the southeast coast of China in 1980. See LARDY, supra note 18, at 41-42.

46 Id. at 16.

47 In the 1950s, some 90% of China's imports were producer goods. This percentage would later drop in the 1960s as China began to import more grain, but overall China's import substitution policies ensured a bias against the import of consumer goods. Id. at 29-32.

48 The People's Bank of China apparently believed that a devaluation was tantamount to a loss of national prestige. Id. at 23.

49 Id. at 21.

50 Id. at 22-23.

51 In 1964, China began converting the import cost to domestic cost by using a premium rate for the yuan. The premium started at 103% in 1964, decreased to 60% in 1975, and increased to 80% from 1977 to 1980. This policy effectively devalued the yuan, and as a result prices on about one fifth of China's imports effectively doubled. The beneficiaries of this devaluation were China's producer goods sector, particularly makers of machinery and other equipment, who could price their goods beneath competing imports. Id. at 22-23.
faced by many centrally planned economies, which was that its overvalued exchange rate ensured that most exports resulted in currency losses. For example, when one of China’s state-run trading enterprises bought textiles from a domestic producer and then exported them, the overvalued exchange rate ensured that when the trading company converted its dollar earnings back into yuan, the amount it received would often be less than the original amount it paid to acquire the textiles. In a market economy, where decisions are based on prices, and prices reflect the actual value of goods, such losses would normally not be allowed to continue. However, in a centrally-planned economy like China, relative costs did not affect production decisions. As a result, exports of surplus goods would continue even as currency losses mounted. The best that China’s trade planners could hope for was to offset export losses with customs revenues and with export profits from China’s more competitive products, such as agricultural goods. Even so, China’s exports continued to create losses up to the 1980s.

From the mid-1960s to the early-1980s, Chinese planners found that the most efficient way to balance its collection of loss-making and profit-making enterprises was through a complex system of exchange rate measures. For example, the 1964 pricing reform mentioned above effectively set up a dual-rate currency: For about 80% of import transactions, the official rate used to convert yuan to dollars was 2.46 (i.e., an enterprise had to pay only 2.46 yuan for every dollar it needed), but for certain imports the rate was a more realistic 5 yuan per dollar. Companies that bought imported goods at the latter rate would have to pay more yuan — about twice as much as those companies that used the former rate. Using a dual rate system allowed state planners to subsidize certain sectors, such as the military, by allowing them to pay for imports at an artificially overvalued yuan rate.

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52 Id. at 25.
53 Id. at 25, 31-32.
54 Id. at 25.
55 Id. at 22.
56 Whole plant imports, machinery, and electronic equipment were the main products priced on this basis starting in 1964. Id. at 22.
57 For example, factories run by China’s military did not have to buy their imports at the devalued renminbi rate (5 per dollar). Preferential treatment for the military would later become embedded in China’s foreign exchange retention system in the 1980s, allowing military-run enterprises to retain 100% of their hard currency earnings. Id. at 23, 55.
C. The Deng Reforms

Under Deng Xiao-ping's leadership, China began to reform its trade and economic policies from 1979, to the early 1980s. In 1979, China established the special economic zones and a joint venture law, and began to shift its trade policy towards export promotion. At the same time, China began to grant more autonomy to trading enterprises. The government scrapped the old system of centralized trading houses. By the mid-1980s, China had several hundred foreign trade companies in operation, and the number reached 1,500 by 1987, and topped 5,000 by 1990.

Perhaps the most critical part of China's trade reforms was the revision of the exchange rate structure. Clearly, Beijing needed a more accessible system of foreign exchange administration in order to encourage exports and foreign investment. Thus, starting in 1979, China began to allow certain enterprises to retain a fraction of their foreign exchange earnings instead of exchanging them back into yuan. The actual amount retained varied depending on the products and industry involved, but in general the retention rate was 15-30%.

In 1985, China expanded this system of foreign exchange retention by opening the first foreign exchange adjustment center (hereinafter called a swap center) in Shenzhen. The swap center offered a kind of crude currency market where selected trading enterprises could either exchange their retained hard currency for yuan, or sell yuan for hard currency.

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58 Gradual reforms to decentralize China's trading system continued in the first half of the 1980s, backed by China's Ministry of Foreign Economic Relations and Trade. MOFERT put forth a five-part trade reform agenda to the State Council in 1984, and the State Council officially sanctioned the reform program on September 15, 1984. See generally CHINA: EXTERNAL TRADE AND CAPITAL, WORLD BANK COUNTRY STUDY 1988 at 21 [hereinafter CHINA: EXTERNAL TRADE AND CAPITAL].

59 LARDY, supra note 18, at 39.

60 Id.

61 WORLD BANK COUNTRY STUDY, supra note 9, at 48.

62 The funds retained were actually held by the Bank of China, and thus could be characterized as an entitlement to use foreign exchange, subject to government oversight. LARDY, supra note 18, at 52.

63 The retention rate was most generous (30% of all earnings) for assembly operations that used imported parts. Most enterprises that sold commodities could only retain a fraction (20-40%) of their earnings above the level they recorded in 1978. Id. at 52-3.


65 Exchanges at the swap centers were governed by complex rules governing the amount that could be traded, the required purpose for the trade, the frequency of exchanges allowed. For an informative background on the early swap center regulations, see generally Hiram E. Chodosh, Swap Centers in the People's Republic of China: A Step Toward Partial Convertibility of Local Currency, 25 INT'L LAWYER 415 (1991).
Expanding the retention system\textsuperscript{66} and allowing limited convertibility marked a key shift in China's ideological stance: no longer would the People's Bank of China act as the sole manager of foreign exchange. China had decided to adjust its incentive structure by allowing companies to manage a share of their own profits.

After the Shenzhen opening, the swap center system expanded quickly. By 1989, there were about 80 swap centers throughout China.\textsuperscript{67} The swap centers became the principal means by which foreign-invested enterprises operated their affairs. They relied on these centers to acquire yuan in order to pay local costs, and to exchange their domestic earnings into dollars for repatriation. Also, all companies needed hard currency to pay for imported goods, particularly components. Thus, the swap centers provided a workable source of hard currency to fund imports. By 1993, the swap centers handled about 80\% of all current account transactions within China.\textsuperscript{68}

The opening of swap centers effectively cemented a dual currency regime within China. The Bank of China handled two exchange rates. First, it set an official rate for the yuan, which was used by tourists\textsuperscript{69} and for priority imports under the state plan.\textsuperscript{70} Second, the bank allowed the swap center administrators to peg a daily swap center rate, which was allowed to float within a limited range. This rate was allowed to depreciate relative to the official rate,\textsuperscript{71} and thus accurately reflected supply and demand. The official rate remained highly overvalued. For example, in 1988, one U.S. dollar bought only 3.7 yuan at the official rate, while at the swap centers

\begin{itemize}
  \item \textsuperscript{66} In the early years of the swap centers, companies in most provinces were allowed to retain 25\% of their earnings in the form of foreign exchange entitlements. Enterprises in Xinjiang province could keep 50\%. The retention rates in the Special Economic Zones (i.e., Shenzhen) and Tibet were 100\%, while Guangdong and Fujian provinces retained 30\%. Priority industries, such as tourism and electronics, were allowed to keep 30-50\% or more. Yowell, supra note 64, at 11.
  \item \textsuperscript{67} LARDY, supra note 18, at 61.
  \item \textsuperscript{69} The official rate was the rate at which tourists had to exchange their hard currency for Foreign Exchange Certificates, the special currency that foreigners had to use while in China. China Removes Controls, supra note 21, at 26.
  \item \textsuperscript{70} NOV. 1993 TREASURY REP., supra note 36, at 23.
  \item \textsuperscript{71} LARDY, supra note 18, at 62.
\end{itemize}
one dollar bought 6 yuan.72 In terms of yuan received per one dollar exchanged, this premium of the swap market rate over the official rate stayed at about 67% in 1988.73 The difference between the two rates then narrowed to about 35% in late 1989,74 and narrowed further to less than 10%75 at the end of 1990. The two rates remained close to each other (roughly 5-10%) up to the beginning of 1992.76 After 1992, the swap center rate then diverged again from the official rate. Thus, in October of 1992, the swap center rate averaged 6.91 yuan per dollar, but the official rate was only 5.55 yuan per dollar, a gap of about 25%.77 The gap increased to about 45% by February of 1993,78 and later peaked at over 80% in June79 before settling back down to about 50% by the end of 1993.80

By using two rates, China realized several trade benefits:

1. **Subsidies to Certain Sectors**

   As noted above, China could protect certain industries by allowing them to pay for imported commodities at the overvalued official rate. The main beneficiaries were certain state-run enterprises and the military, who in effect were allowed to pay much less than the actual price for imported goods.81 The central bank absorbed a currency loss on these transactions.

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72 Id. at 65.
73 Id.
74 In late 1989, the official rate was devalued to 4.2 yuan per dollar while the swap market rate was about 5.7 yuan. Id. The figure of 35% is extrapolated from Lardy's data: In late 1989, for every dollar paid in, a person would receive roughly 35% more yuan in return if he exchanged his dollar at the swap center rate compared to the official rate.
75 In late 1990, the official rate was devalued from 4.2 yuan per dollar to 5.2 yuan per dollar. Shortly thereafter the swap market rate in Shanghai stood at only 5.3 yuan per dollar. In other cities the swap market rate ranged from 5.5 to 5.7 yuan per dollar. Id. at 65.
76 Exact data on the swap center rates are difficult to locate, but Peter Harrold and Rajiv Lall of the World Bank have published a graphic based on IMF data that shows the swap center rate holding at under 6 yuan per dollar from the end of 1990, up to the beginning of 1992. (Unfortunately, the graphic does not state exact figures for the two rates). During this time, the official rate was 5.2 to 5.7, according to official Chinese statistics. See 1993 IMF Int'l Fin. Stat. Y.B. 279. Thus, the difference between the two rates did not vary much more than about 5-10%. See Peter Harrold & Rajiv Lall, *China: Reform and Development in 1992-93*, 215 World Bank Discussion Papers 15 (1993).
77 DEC. 1992 TREASURY REP., supra note 36, at 32.
78 Harrold & Lall, supra note 76, at 16.
79 On June 1, 1993, China lifted restraints on the swap center rate and the yuan immediately depreciated to about 10.5 yuan per dollar. The official rate was about 5.77 per dollar. Thus, the premium of yuan received for each dollar was about 81%. See NOV. 1993 TREASURY REP., supra note 36, at 25.
80 The gap between the swap center rate and the official rate was 51% on November 10, 1993. Id.
81 The subsidy amounted to the difference between the swap center rate and the official rate. Thus, in 1988, importers enjoying the subsidy would only have to pay about 3.72 yuan for every one dollar worth of imports they purchased. This was a large savings over the market rate of 6 yuan per dollars worth of
Allowing some enterprises to use the official rate for imports shielded these enterprises from world prices, and thus helped to prop up many of China's more inefficient producers. Chinese policy makers needed this so-called "air-lock" to protect the domestic economy from effects of sudden price competition. The alternative choice was to allow a steep devaluation of the yuan, which would have forced all Chinese enterprises to pay market rates for their imports and would have sparked inflation, a step China was unwilling to take.

2. **Taxes on Foreign Exchange Transactions**

The dual rate system also enabled China to levy a hidden tax on currency trades. For example, in 1988, the Bank of China had to pay only 3.72 yuan (not the swap center rate of about 6 yuan) for each 1 U.S. dollar it purchased, a savings of about 38%. Thus, the bank could add to its foreign exchange reserves by forcing trading enterprises to "sell" part of their hard currency earnings at the official rate rather than the swap center rate. In particular, the People's Bank of China could target foreigners by forcing them to register their incoming capital at the official rate and repatriate profits at the swap market rate. Tourists also had to use the official rate to buy local currency.

Though the tax on currency exchanges could be harsh on foreign-invested enterprises, ultimately it extended to all exporters. By 1993, China had reformed its retention rate structure and required almost all trading enterprises to surrender 20% of their foreign currency earnings at the official rate, while the government had an option to buy 30% of the earnings at the swap center rate. The trading enterprises could keep the remaining 50% in a foreign exchange credit account. In effect, 80% of the trading enter-

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82 "Air-lock" is the term used by economists to describe the almost total shield of protectionism existing between China's economy and the world economy prior to the late-1970s and 1980s. Remnants of the "air-lock" policies persisted through the 1980s, and to the present. See CHINA: EXTERNAL TRADE AND CAPITAL, supra note 58, at 25-26.

83 LARDY, supra note 18, at 65.


86 Nov. 1993 TREASURY REP., supra note 36, at 23.
prise's trade revenue would be either held in a foreign currency account or converted to yuan at an approximate market rate (the swap center rate), while the Bank of China realized a hidden exchange tax on the 20% portion that it forced the trading enterprise to exchange at the official rate.87

D. International Response to China's Currency Practices

China submitted its application to join GATT in July 1986, and in March 1987, the GATT set up a working party to handle China's bid.88 From the beginning, no one expected China's accession to move quickly.89 In 1985, China had launched its reform program for urban areas, which included the introduction of two-tiered pricing and the decentralization of enterprise management.90 Once the talks with GATT began, information about the extent of Beijing's reforms was hard to come by, and fact finding proved to be a slow process.91

It is difficult to discuss details of China's GATT bid because the working party's negotiations were private. Press reports and comments by the parties involved, particularly the U.S., give only an indication of the GATT talks. It is clear, however, that prior to the Tiananmen incident, the working party focused mostly on broad reform issues such as China's state sector, subsidies, and the transparency of regulations.92 The problem of currency controls apparently did not receive much attention until the last two years of the Uruguay Round.93 The main criticisms, coming both from within the working party and from U.S. policy makers, are described below:

87 This was a significant amount of revenue, given that China's 100 or so swap centers were handling about 80% of all current account transactions in 1993. See China Unifies Exchange Rates, supra note 68, at 11.
88 See generally supra note 3.
89 See GATT Rejects, supra note 15, at 1477.
90 The Third Plenary Session of the 12th Central Committee of the Communist Party adopted the "Decision on Reform of the Economic Structures" on October 20, 1984. This was the seminal document upon which China's reform program was introduced in urban areas starting in 1985. See WORLD BANK COUNTRY STUDY, supra note 9, at 42-43.
91 China's responses to questions from working party members were apparently vague and often conflicted with information provided by foreign companies operating in China. See GATT Rejects, supra note 15, at 1477.
92 See GATT Working Group, supra note 39, at 253.
93 It was in 1992, and 1993, that the swap center rate of the yuan and the official rate began to diverge. Supra notes 77-80. Press reports indicate that China answered questions on its foreign exchange allocation system in March and October 1993. See, e.g., Talks on China's GATT Membership End, supra note 40, at 490; Specific Problems Facing China for GATT Re-entry Are Outlined, 10 INT'L TRADE REP. (BNA) 1690 (Oct. 6, 1993).
1. Foreign Investors Lose Out

Foreign investors were among the loudest critics of China's swap center system. Initially, the swap centers helped to solve a serious liquidity problem by providing a mechanism through which investors could repatriate their yuan profits. This was particularly important for those investors who were manufacturing goods in China to sell to Chinese consumers. Most of their earnings were in local currency and they had little or no foreign currency earnings to help pay for needed imports, and thus no way to acquire hard currency for repatriation.94

The big problem, however, was that the swap centers would literally run out of hard currency in times of heavy demand.95 This created enormous tension for China's monetary authorities. If the People's Bank of China tried to limit the outflow of hard currency by restricting activity at the swap centers, black market money traders would simply take over a larger part of the currency market, and the result would be a sharp devaluation of the black market yuan rate. This is exactly what happened in mid-1993.96 By June of 1993, increasing restrictions on swap center trades led to a general shortage of U.S. dollars, which pushed the black market rate to above 10 yuan per U.S. dollar. At the same time, the swap center rate was 40% overvalued at 8.135 yuan to the dollar, and the official rate was a totally unrealistic 5.7 per dollar.97 Unable to compete with the black marketers, and facing a shortage of U.S. dollars, the swap centers severely restricted exchanges.98 This left the foreign-invested companies in a bind. They were legally prohibited from trading money on the black market, but there was nowhere else to acquire hard currency.99 Moreover, the extent of this problem was not short-term; a shortage of hard currency had been

94 China Removes Controls, supra note 21, at 26.
95 Increased demand is evidenced by the increased turnover at the swap centers. In 1992, the swap centers handled US$ 26 billion worth of transactions, a fourfold increase over the US$ 6.2 billion in exchanges handled in 1988. China Removes Controls, supra note 21, at 26.
96 See id.
98 See China Removes Controls, supra note 21, at 26.
99 Id. Many foreign companies did turn to the black market to stay in business. "Finding dollars became so competitive that foreign companies started dispatching local employees with checkbooks and portable phones to cities across China in search of any black-market currency deals they could find." Id.
building for about five months. Trading companies, including most foreign-invested companies, had difficulties getting hard currency from the swap centers because administrators were routinely rejecting applications for yuan-to-U.S.$ exchanges.

In June of 1993, the government finally caved in and devalued the swap center rate to over 10 yuan per dollar, allowing it to approach the black market rate. While this move allowed the swap centers to open again, it was a hollow victory. China’s policy of trying to close the gap between the official rate and the swap center rate had spun out of control and the gap had actually widened. In effect, China’s black market had momentarily wrested control away from the center, and forced a devaluation of the swap center rate. In the process, foreign investors learned that the swap centers could not always be counted on.

2. Pressure from Foreign Governments

Foreign governments, particularly the U.S., were another critic of China’s currency system. As mentioned above, the U.S. Department of Treasury first cited China for “manipulating” its currency in November 1992, and continued to make this claim throughout 1993. The U.S. was concerned because its 1992 trade deficit with China was $18.3 billion, and the 1993 deficit was expected to increase 26% to $23.1 billion. The EC’s bilateral trade with China had shifted dramatically from a 2.3 billion ECU surplus in 1985, to a 10 billion ECU deficit in 1991. Within the GATT working party, the representatives from the E.C. and other developed nations generally echoed U.S. complaints about China’s trade practices.

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100 Facing pressure to depreciate the swap center rate, China capped this rate at 8.2 yuan per dollar in February 1993, which caused the swap centers to reduce the total volume of transactions. This forced many foreign exchange transactions onto the black market. See Nov. 1993 Treasury Rep., supra note 36, at 25.


103 Id.

104 Id. at 22.


106 See Talks On China’s GATT Membership End, supra note 40, at 490.
For foreign governments, the chief concern was that China’s dual-rate currency system acted like a new barrier to imports. In order to acquire hard currency at a swap center, the trader first had to state why it needed the money. The State Administration of Exchange Controls (SAEC), which administers the swap centers, had wide discretion to turn down applications for foreign exchange.\(^{107}\) GATT participants were suspicious because China was applying this form of import control on top of existing measures. In effect, even applicants who had already procured an import license could be turned down by the SAEC. Moreover, the SAEC had published only general guidelines on which exchanges would be allowed,\(^ {108}\) and access to more detailed information was restricted. In particular, trading enterprises generally had no access, or very limited access, to the complete SAEC regulations.\(^ {109}\)

Complaints that China’s swap centers were being used to restrict imports began to emerge from the GATT negotiations in 1993. Delegates from the U.S., Canada, Australia, and the Philippines were quoted in the press as opposing China’s two-tiered exchange rate.\(^ {110}\) In response, China’s delegates at the GATT talks promised that China would achieve a single exchange rate of the yuan within five years, and convertibility shortly thereafter.\(^ {111}\) Shortly after the talks ended, China confirmed that it would eliminate its two-tiered currency system in order to join GATT.\(^ {112}\)

China announced that it would unify its official and swap center rates as of January 1, 1994.\(^ {113}\) Whether this reform will aid China’s accession to GATT is considered in Part IV below. First, however, it is important to consider the legal rules and norms that exist within GATT and the IMF relating to currency practices. Thus, Part III below will explain the GATT-IMF legal framework and attempt to apply this framework to China’s former dual-rate currency. In effect, Part III examines a hypothetical situation: Imagine that China maintained a dual-rate currency and was admitted to GATT, would the GATT-IMF rules be applicable in policing

\(^ {107}\) Nov. 1993 TREASURY REP., supra note 36, at 24.

\(^ {108}\) Id.

\(^ {109}\) “Generally, China’s foreign exchange system is not transparent. China does not allow public access to the regulations governing foreign exchange, including the regulations governing China’s swap centers.” Id.

\(^ {110}\) Talks On China’s GATT Membership End, supra note 40, at 490.

\(^ {111}\) Latest GATT Talks on China’s Readmission End with No Agreement, Delegates Say, 10 INT’L TRADE REP. (BNA) 911 (June 2, 1993) [hereinafter Latest GATT Talks].


\(^ {113}\) Id.
China's dual-rate currency practices? The GATT working party faced this hypothetical question when it was deciding whether to let China into GATT with its dual-rate currency, or delay China's entry pending a currency reform.

III. THE GATT-IMF FRAMEWORK APPLIED TO CHINA'S DUAL-RATE REGIME

A. Introduction

If China was a GATT member, using GATT rules to police China's dual-rate currency would be difficult because GATT has long granted preferential treatment to developing nations. The leniency towards developing nations is not new. Since the end of the Tokyo Round of multilateral talks in 1979, preferential treatment of developing nations has been a trend within GATT. The Articles of Agreement of the IMF also grant lenient treatment to developing nations. Thus, in most disputes involving

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114 Article XVIII, Governmental Assistance to Economic Development, outlines protective measures GATT members can take, and is targeted at "those contracting parties the economies of which can only support low standards of living and are in the early stages of development." GATT CHARTER art. XVIII, ¶ 1. In 1979, GATT members accepted Part IV into the charter. Part IV distinguishes between "developed" and "less developed" contracting parties, and provides special leniency to the latter group. There is no formal definition of a "less developed" GATT member. Instead, members that feel entitled to this status can simply claim it. JACOBSON & OKSENBERG, supra note 2, at 94. Part IV of GATT includes several provisions intended to limit the less developed nation's obligations under GATT. Thus, Article XXXVI, Principles and Objectives, sets the tone of Part IV: "The contracting parties... (c) noting, that there is a wide gap between standards of living in less-developed countries and in other countries;... (f) noting that the CONTRACTING PARTIES may enable less-developed contracting parties to use special measures to promote their trade and development; agree as follows." GATT CHARTER art. XVIII, ¶ 1. Part IV then goes on to state the principle that the developed members do not expect less-developed members to offer reciprocity in exchange for commitments to reduce or remove tariffs and other barriers. Thus, the less developed members are not expected, in trade negotiations, "to make contributions which are inconsistent with the individual development, financial and trade needs, taking into consideration past trade developments." GATT CHARTER art. XXXVI, ¶ 8.

115 The Tokyo Round, 1973-1979, focused on the establishment of "differential and more favorable treatment" for developing nations, a movement which was intended to expand trade of developing nations by allowing them to grant import preferences to members of their choice, and to avoid GATT's reciprocity requirements with developed nations. See OLIVER LONG, LAW AND ITS LIMITATIONS IN THE GATT MULTILATERAL TRADE SYSTEM 89-106 (1985).

116 Under Article IV, the IMF has authority to "exercise firm surveillance" over the exchange rate policies of its members, but it also must "respect the domestic social and political policies of members." SECOND AMENDMENT TO THE ARTICLES OF AGREEMENT OF THE IMF art. IV, § 3(b) [hereinafter IMF ARTICLES OF AGREEMENT]. Article XIV recognizes the IMF's limited reach by allowing an incoming member to restrict the convertibility of its currency for an unspecified "transitional" period, decided upon by the member nation. Article XIV, § 2 reads:
monetary issues, a developing nation like China can fend off criticism by pointing to GATT\textsuperscript{117} and IMF\textsuperscript{118} provisions in support of its position.

If admitted to GATT as a less-developed nation,\textsuperscript{119} China would likely be able to use lenient GATT and IMF rules to its advantage. However, this does not mean that China could act with impunity. While the GATT charter and GATT rulings do not specifically outlaw dual-rate currency regimes,\textsuperscript{120} they do limit a nation’s ability to restrict imports for the purpose of protecting its balance of payments.\textsuperscript{121} The IMF charter also limits when a country can restrict payments related to international trade.\textsuperscript{122} Thus, as a starting point, it should be emphasized that both GATT and the IMF have rules that would restrict how China could conduct its foreign exchange practices as a GATT member. These rules are considered in more

\begin{footnotesize}
A member that has notified the Fund that it intends to avail itself of transitional arrangements under this provision may, notwithstanding the provisions of any other articles of this Agreement, maintain and adapt to changing circumstances the restrictions on payments and transfers for current international transactions that were in effect on the date on which it became a member.

\textsuperscript{117} For example, GATT Art. XVIII shields developing countries from harsh consequences should they enact trade barriers. Section B of Art. XVIII allows wide-ranging import restrictions when a nation’s monetary reserves are facing “a serious decline,” or when a nation “with inadequate monetary reserves” needs to achieve a “reasonable rate of increase in its reserves.” GATT CHARTER art. XVIII, § B. Under § B, a less developed nation that enacts import restrictions will have to consult with GATT’s Balance of Payments Committee on the issue of its monetary reserves position. However, any other nation that is adversely affected by the less developed member’s import restrictions has in principle no right to compensation or retaliation under Art. XVIII, § B. \textit{The Relationship, supra} note 19, at 380.

\textsuperscript{118} See IMF ARTICLES OF AGREEMENT, supra note 116.

\textsuperscript{119} China intends to be admitted as a less developed member. \textit{China Files Membership Application, Council Hears U.S. Farm Trade Charges Against Japan}, 3 INT’L TRADE REP. (BNA) 915 (July 16, 1988). GATT has no formal definition of a less developed member. See JACOBSON AND OKSENBERG, supra note 2, at 94.

\textsuperscript{120} The GATT charter is silent on multiple currency practices. The IMF Articles of Agreement mentions multiple rate practices in Art. VIII, but does not prohibit them: “No member shall engage in, or permit any of its fiscal agencies . . . to engage in, any discriminatory currency arrangements or multiple currency practices . . . except as authorized under this Agreement or approved by the Fund.” IMF ARTICLES OF AGREEMENT art. VIII, § 3. Art. VIII goes on to state that if a member is using discriminatory currency practices or multiple currency practices when it becomes an IMF member, it can keep these measures in place under the transitional arrangements of Art. XIV. Nations using Article XIV face annual reports by the IMF on their currency measures, and agree to remove such barriers once their monetary situation improves. IMF ARTICLES OF AGREEMENT art. XIV, §§ 2, 3.

\textsuperscript{121} GATT Art. XVIII(B) provides for oversight of a country’s import restrictions taken for balance of payments reasons. This procedure serves to make sure that any restrictions applied do not violate GATT rules. GATT CHARTER art. XVIII, § B.

\textsuperscript{122} The IMF limits on restrictions on payments. A nation entering the IMF can elect to take advantage of the transitional arrangements under Art. XIV, and thereby keep in place any restrictive currency practice. A nation taking this step will be subject to annual review by the IMF, and the IMF may propose that the nation eliminate the restriction. IMF ARTICLES OF AGREEMENT art. XIV, § 3.
\end{footnotesize}
detail below, but first it is important to understand the shared responsibilities of GATT and the IMF over monetary issues.

B. **GATT and the IMF's Historic Compromise on Jurisdiction**

GATT and the IMF both oversee monetary issues that affect trade. Some degree of cooperation is necessary for both organizations since international trade, by definition, involves the exchange of goods for payment. Thus, GATT has an interest in ensuring that payment mechanisms used by GATT members do not restrict trade flows. The IMF has the same interest. In practice, GATT and the IMF’s shared responsibility has allowed GATT to avoid the task of creating an independent body of rules and precedents to govern exchange rate policies.

GATT’s limited activity in this area is largely an accident of history. In July 1944, just weeks after the Normandy landings, 45 nations met at the Bretton Woods Conference to tackle one of the most pressing economic issues at the time: exchange rate stability. The Bretton Woods talks produced a charter for the International Monetary Fund (IMF), but at that time a global trade framework was still being planned.

The GATT charter, ratified in October 1947, was far less ambitious than the IMF. GATT was originally viewed as a means to encourage trade concessions through multilateral tariff cuts. Unlike the IMF, GATT initially had no formal organizational structure, and did not have a

123 The Relationship, supra note 19, at 366.
124 "[GATT] Contracting parties shall not, by exchange action, frustrate the intent of the provisions of this Agreement." GATT CHARTER art. XV, ¶ 4 & amend. art. XV.
125 Among the purposes established by Art. I of the IMF Articles of Agreement is this one: "To facilitate the expansion and balanced growth of international trade . . . ." IMF ARTICLES OF AGREEMENT art. I, ¶ ii.
126 The Articles of Agreement of the World Bank were also agreed to at the conference. The IMF was officially established on Dec. 27, 1945, upon the approval of 29 governments. See generally MARGARET GARRITSEN DE VRIES, THE IMF IN A CHANGING WORLD: 1945-85, at 3-20 (1986).
127 Roessler notes that the U.S. Dept. of Treasury initially proposed setting up a post-war monetary institution with authority over both trade and monetary affairs. However, in the post-war era, the U.S. split up its reconstruction duties by granting the State Department responsibility for world trade policy and the Department of Treasury responsibility over world monetary affairs. Treasury would later back off its proposal to give the IMF broad authority over trade, and the State Department would formulate a world trade body (the ITO) that respected the IMF's jurisdiction over monetary issues. The Relationship, supra note 19, at 365 & nn.1, 2.
128 See generally U.S. DEPT OF STATE, PUB. NO. 2983, ANALYSIS OF THE GENERAL AGREEMENT ON TARIFFS AND TRADE (1947) (discussing the broad tariff reductions established by the original GATT ratification).
permanent meeting place. GATT only became the world’s *de facto* trade body after the U.S. Congress refused to support the much more ambitious International Trade Organization (ITO) in 1950.

While the IMF started as a much more established organization than GATT, the U.S. and its allies essentially made a pragmatic decision to allow the IMF and GATT to oversee separate jurisdictions. The IMF would handle monetary issues, and GATT would handle trade. Of course, the two bodies had to cooperate in some matters, namely restrictions against payments (i.e., controls on the spending of hard currency for foreign goods). The GATT contracting parties knew that payments restrictions could be used as a trade barrier, but at the same time they respected the IMF’s edict to oversee international monetary issues. Thus, it was logical that both organizations would play a role in overseeing monetary restrictions that were used as trade barriers. They both had an interest in this area.

The drafting parties believed that currency measures were a critical issue. The U.S. State Department, for example, frequently warned that "exchange restrictions *could* destroy the freedom [to trade] which it is the major purpose of the [ITO] proposals to encourage." (Italics in original). The concern about currency restrictions stemmed from a dilemma: the drafting parties knew that quantitative restrictions on trade (i.e., import quotas) were the most protectionistic of trade measures, but they also knew that in the post-war era some nations would need quantitative restrictions in order to protect their monetary reserves. Thus, the contracting parties had to walk a fine line. In drafting a charter for world trade, they

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129 GATT did not have a formal structure in its first ten years. The initial GATT sessions were informal meetings, basically carried over from the preparatory committee of the International Trade Organization (ITO). In late 1954, Geneva became the *de facto* site for the organization. See generally ROBERT E. HUDEC, THE GATT LEGAL SYSTEM AND WORLD TRADE DIPLOMACY 60-65 (1975).


131 A 1947 State Department commentary lays out the basic premise: "Quantitative restrictions, which are the concern of the [International Trade Organization], and exchange restrictions, which are the concern of the International Monetary Fund, are equally effective methods of controlling trade. It is essential, therefore, that these two organizations work hand in hand." U.S. DEP’T OF STATE, PUB. NO. 2950, THE GENEVA CHARTER FOR AN INTERNATIONAL TRADE ORGANIZATION: A COMMENTARY 8 (1947) [hereinafter U.S. DEP’T OF STATE, PUB. NO. 2950].

132 *Id.*

133 *Id.* at 6-7.

134 U.S. DEP’T OF STATE, COMMERCIAL POLICY SERIES, PUB. NO. 2591, NEW HORIZONS FOR WORLD TRADE 8 (1946).

135 *Id.* at 6-7.
had to disapprove of quotas as a fundamental principle, but allow some limited quotas for nations that were facing monetary crises.

For the last forty years, GATT's policy of deferring to the IMF on issue of payments has allowed it to sidestep the task of creating and enforcing legal precedents in this area. Thanks to the framework of shared responsibility, GATT has never been forced to take an independent stand on currency matters. Instead, GATT has relied on IMF input. Moreover, GATT and the IMF's cooperation in this area has remained informal. When both the GATT and the ITO were still under discussion, the U.S. assumed that whatever trade organization that emerged would "work hand in hand" with the IMF. This "hand in hand" relationship was never clearly defined in terms of policy coordination. Today, it remains a target of concern among trade analysts.

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136 A U.S. State Dept. commentary expressed the overall policy with regards to drafting of the ITO charter: "The Geneva Charter [of the ITO] condemns quantitative restrictions in principle. It does not abolish them, for their use is sometimes legitimate; but it confines them to exceptional circumstances which are narrowly defined, carefully safeguarded, and subject to international scrutiny and control." Id. at 6.

137 Under the ITO charter, three general rules governed when a nation could use the balance of payments exception to impose import restrictions. First, the country in question could use restrictions "only to the extent necessary" to keep a reasonable amount of monetary reserves. Second, the country had to lift the restrictions once its monetary reserves reached a reasonable level. Third, a country imposing such restrictions had to consult with the ITO. See id. at 7.

138 Roessler describes the relations between GATT and the IMF as "cordial and intellectually fruitful," but points out that "there is nothing that could be described as policy coordination between the governing bodies of the two institutions." The Relationship, supra note 19, at 385. The reason for the informal relations is partly historic. In 1948, the Interim Commission for the International Trade Organization (ITO) drafted an agreement to coordinate relations with the IMF. Under the "Relations Between the ITO and IMF" agreement, each organization was obliged to consult with the other and exchange information. Additionally, the agreement provided for reciprocal representation and participation of the members in one organization in meetings of the other. When the ITO was stillborn, the idea for a formal agreement linking the IMF to a world trade body was deemed unnecessary. Instead, GATT and the IMF agreed to cooperate informally. Id at 385 & n.58.

139 Commentary from the State Dept. demonstrates that the U.S. felt that cooperation between the IMF and the ITO would be a natural outgrowth of their relationship. The State Dept. did not attempt to define this cooperative structure, but felt that the two bodies would collaborate on trade issues relating to balance of payments levels. See U.S. DEP'T OF STATE, PUB. NO. 2950, supra note 131, at 7-8.

140 For example, Pierre-Louis Girard, Swiss ambassador to GATT, has commented that GATT is still "paying today" for decisions made over 40 years ago to split jurisdiction between GATT and the IMF. In particular, the GATT-IMF relationship has failed to establish "a meaningful policy coordination" with respect to trade restrictions taken for balance of payments purposes. Pierre-Louis Girard, The Relationship Between the World Trade Order and the International Monetary System: A Comment, in 5 THE NEW GATT ROUND OF MULTILATERAL TRADE NEGOTIATIONS: LEGAL AND ECONOMIC PROBLEMS 387, 389, 391 (Ernst-Ulrich Petersmann & Meinhard Hilf eds., 1988).

141 Id.
C. **GATT Article XV and the Structure of GATT-IMF Cooperation**

Article XV of the GATT charter outlines the GATT and IMF's coordinated policy for overseeing exchange rate arrangements. The principle of Article XV is that currency matters fall within the jurisdiction of both organizations. As a 1954 report on the GATT-IMF relationship concluded, "in many instances it is difficult or impossible to define clearly whether a government measure is financial [i.e., monetary] or trade in character and frequently it is both."\(^{142}\)

Article XV explains the shared responsibility over exchange rate and balance of payments issues:

In all cases in which the CONTRACTING PARTIES are called upon to consider or deal with problems concerning monetary reserves, balances of payments or foreign exchange arrangements, they shall consult fully with the International Monetary Fund. In such consultations, the CONTRACTING PARTIES shall accept all findings of statistical and other facts presented by the Fund.\(^{143}\)

In effect, this provision allows the GATT contracting parties to avoid ruling on a member's exchange rate mechanism pending a factual analysis from the IMF.

Note that Article XV offers very little in the way of guidelines. It does not tell GATT members what sort of currency mechanisms are permitted. Article XV merely states that "Contracting parties shall not, by exchange action, frustrate the intent of the provisions of this Agreement."\(^{144}\) (emphasis added). Article XV does not attempt to define the "intent" of the GATT charter, nor does it suggest how exchange rate actions might frustrate this "intent." GATT's deferral to the IMF is supposed to illuminate technical issues related to currency mechanisms, but it remains GATT's duty to decide when a nation's exchange actions violate the GATT charter.

One problem with deferral is that the IMF does not have a reciprocal obligation to consult with GATT on trade issues that affect monetary


\(^{143}\) GATT CHARTER art. XV, §2.

\(^{144}\) GATT CHARTER art. XV, §4.
affairs. In creating the post-war institutions, the world powers initially desired that the IMF and the ITO would establish formal ties to coordinate their policies. But when the ITO failed to materialize, it was thought at the time that GATT did not need a formal relationship with the IMF. In lieu of formal ties, GATT would rely on the IMF as a provider of information. The IMF, however, had no obligation to accept GATT’s findings on trade matters.

IMF independence on monetary affairs has translated into a world where the IMF has created its own standards and exceptions relating to currency practices. For example, regarding multiple-rate structures, Article VIII(3) of the IMF’s Articles of Agreement states the Fund’s general disapproval of this practice:

No member nation shall engage in, or permit any of its fiscal agencies . . . to engage in, any discriminatory currency arrangements or multiple currency practices, except as authorized under this Agreement or approved by the Fund.

In practice, the IMF has never clearly delineated when exactly a country can use multiple rates. It has struggled with the issue, and has ultimately decided to allow some multiple rate regimes. Thus, in a 1981 decision, the executive board of the IMF ruled that multiple rate practices would be tolerated if they are maintained to protect a shortfall in the nation’s balance of payments. A nation imposing multiple rates would have to promise that the practice will be temporary, and that it will not

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146 Id.
147 Id. at 644.
148 IMF ARTICLES OF AGREEMENT art. VIII, § 3.
149 In a 1981 decision, the IMF established the general conditions under which a multiple exchange rate regime would be allowed:

[The Fund will be prepared to grant approval of multiple currency practices introduced or maintained for balance of payments reasons provided the member represents and the Fund is satisfied that the measures are temporary and are being applied while the member is endeavoring to eliminate its balance of payments problems, and provided they do not give the member an unfair competitive advantage over other members or discriminate among members.

150 Id.
create "an unfair competitive advantage over other members or discriminate among members." 151

In a dispute involving Article XV, GATT must rely on statistical information provided by the IMF, but the IMF may have already agreed to provide special leniency to the country in question. On a procedural level, this framework of GATT-IMF cooperation requires GATT to import a broad range of IMF information. 152 The relative weight of the IMF's opinions has never been clarified. In practice, the IMF has often been sensitive about reporting on a nation's monetary situation, and thus tends to shy away from offering concrete opinions. 153 Sometimes the IMF puts forth a recommendation. 154 But it often favors a status quo approach and does not make recommendations to GATT. 155 Ultimately, the Article XV framework has left GATT with little independent authority to decide trade disputes caused by monetary policies.

1. China's Dual-Rate Currency Applied to Article XV

If China had been admitted to GATT before 1994, Article XV would have required GATT to weigh the IMF's input on China's dual-rate currency mechanism. The process of the Article XV examination would have been lengthy due to the need to collect data. Moreover, GATT has special procedures for less-developed nations which are designed to ease their burden in facing periodic review sessions. 156 These procedures, contained in Article XVIII(B), serve to lengthen the data collection period by allowing

151 Id.
152 Art. XV states in part: "[GATT] shall accept the determination of the Fund [on the nation's level of monetary reserves], and as to the financial aspects of other matters covered in consultation in such cases." GATT CHARTER art. XV, ¶ 2.
153 As Roessler noted. "The lack of procedures guaranteeing confidentiality has made the [IMF] reluctant to suggest in consultations with GATT alternative balance-of-payments measures (in particular devaluations or capital controls)." Roles of the GATT and the IMF, supra note 145, at 650.
154 Id. at 647.
155 Id.
156 Most developing nations that impose import restrictions for balance of payments reasons tend to have long-term problems. Thus, they have asked for, and been granted, special leniency with regards to the timing of consultations with GATT. Frieder Roessler, The GATT Declaration on Trade Measures Taken for Balance-of-Payments Purposes: A Commentary, 12 CASE W. RES. J. INT'L L. 383, 395 (1980) (hereinafter The GATT Declaration). Article XVIII(B), introduced in 1955, extended the period between regular consultations from one year (under Article XII) to two years for nations that adopted protective measures allowed under Article XVIII(B). GATT CHARTER art. XVIII, § B, ¶ 12(b).
less-developed members to submit to consultations on their balance of payments situation every two years instead of annually.\textsuperscript{157}

As a GATT member China would have potentially faced several Article XV complaints under its dual-rate structure. Part II above points out the nature of these complaints. First, a nation could argue that China’s dual-rate structure had served to unfairly subsidize many of China’s state-run industries. Second, China had often applied the dual rates in a way that taxed foreign exchange transactions and restricted imports. A GATT member could have argued that either or both of these results “frustrate the intent” of the GATT charter, and thus could have pursued a trade complaint against China based on Article XV.

However, the initial difficulty with these complaints is that GATT could only examine China’s “foreign exchange arrangements” \textit{in cooperation} with the IMF. The basis for such an investigation would be IMF information, including data on exchange rates and balance of payments. The investigation itself would be a series of multilateral talks open to any GATT member that wanted to participate on the Balance of Payments Committee.\textsuperscript{158}

It is likely that China would benefit by such a process. The GATT consultation mechanism blunts any single member’s ability to pursue trade actions against another member. This, of course, is one object of multilateralism. However, in practice the party bringing the complaint must rely on a key external variable: the willingness of the IMF to cooperate.\textsuperscript{159} In the past, the IMF has often not been willing to offer recommendations about a nation’s monetary situation because it fears that news leaks might lead to adverse market reactions.\textsuperscript{160} Often the IMF simply reports to GATT that “it has no alternative measures to suggest.”\textsuperscript{161} Thus, while the goal of the GATT-IMF framework is to encourage a nation to adopt corrective measures, the sensitivity of foreign exchange matters makes it difficult for either GATT or the IMF to be explicit about the solutions needed.\textsuperscript{162}

For the GATT member bringing a complaint against China, another unpredictable issue would be the extent to which information other than IMF data would be incorporated in the fact-finding process. For example, if

\begin{thebibliography}{9}
\bibitem{157} Id.  
\bibitem{158} The Relationship, supra note 19, at 380.  
\bibitem{159} Girard, supra note 140, at 391.  
\bibitem{160} Roles of the GATT and the IMF, supra note 145, at 650.  
\bibitem{161} Id. at 650 & n.77.  
\bibitem{162} The GATT Declaration, supra note 156, at 392.  
\end{thebibliography}
China needed to supply data to the IMF or to GATT, China’s performance in the Uruguay Round suggests that this itself would be a drawn-out process.\textsuperscript{163} It is also unclear how much GATT’s Balance of Payments Committee would rely on outside information, such as reports provided by the U.S. Treasury or other GATT members.

A final uncertainty would be the conclusion of the Balance of Payments Committee, which would incorporate any input from the IMF. In practice, the shared responsibility of GATT and the IMF within Article XV has insured that conclusions from the Balance of Payments Committee remain informal and diplomatic. An example is provided by Frieder Roessler, Senior Counsel in the GATT Legal Office. Roessler points out an actual conclusion from the Balance of Payments Committee, in which he has replaced the nation’s name with the letter A:

\begin{quote}
The Committee welcomed the trend toward a progressive relaxation in the application of A’s import restrictions. It noted the view of the [IMF] that the overall restrictiveness of the import regime did not go beyond what was necessary to prevent a decline in A’s international reserves. It also noted the relatively favourable prospects for A’s balance of payments. The Committee noted with satisfaction the determination of A’s authorities to continue relaxing remaining restrictions…\textellipsis{164}
\end{quote}

The purpose of the Balance of Payments Committee, as evidenced here, is to put forth broad conclusions on whether the nation’s import restrictions are allowable under the GATT charter given the nation’s monetary and balance of payments situation. These conclusions do not clearly indicate the facts upon which they are based.\textsuperscript{165} In a 1975 report, the Committee explained that it does not want to state exactly which trade re-

\textsuperscript{163} In the Uruguay Round, China answered an enormous number of questions on its trade practices. JACOBSON & OKSENBERG, supra note 2, at 96. However, many of China’s answers were apparently insufficient, prompting more questions and delays. See, e.g., Latest GATT Talks, supra note 111, at 911; Talks on China’s GATT Membership End, supra note 40, at 490; Talks on Accession to GATT Seem Unlikely to Lead to Much Progress, 10 INT’L TRADE REP. (BNA) 445 (Mar. 17, 1993).

\textsuperscript{164} The GATT Declaration, supra note 156, at 397.

\textsuperscript{165} Id.
restrictions are allowable because these "could be taken by contracting parties as a carte blanche for imposing measures within the limits specified."166

Thus, in the case of China's dual-rate structure, the success or failure of trade complaints brought under Article XV would have depended on a number of uncertain variables. Of particular concern is the nature of the fact-finding process. The following section examines the importance of IMF fact-finding on monetary reserves, and how the IMF's inconclusive data on China's monetary reserves would probably make it difficult to pursue an Article XV complaint if China was a GATT member.

D. Applying Article XV: The Balance of Payments Exception

The GATT charter provides an exception to the Article XV rule that monetary restrictions "shall not frustrate the intent" of the charter. Article XV states that in examining any trade restrictions enforced for balance of payments reasons, the IMF should determine whether a country is suffering "a serious decline" in its monetary reserves, "a very low level" of monetary reserves, or "a reasonable rate of increase" in its monetary reserves, in accordance with Articles XII and XVIII(B). In effect, monetary reserves and balance of payments provide the same information. Both figures reflect a nation's trade imbalance. In other words, they show how much hard currency a nation is spending on goods and services versus how much hard currency it is taking in.167 A sharp drop in a nation's monetary reserves, as evidenced by a declining balance of payments, is an indicator that the nation needs to increase its earnings of hard currency. One way to do this is to restrict overall spending on imports.

GATT's balance of payments exception under Article XV allows a nation suffering a "serious decline" or a "very low level" of monetary reserves to implement import quotas in order to protect its monetary situation. This exception is based on the assumption that if a nation restricts imports of certain goods through a quota, then it will reduce overall spending of hard currency. As noted in the two sections below, this assumption is no longer valid for developed nations, but it is still applicable for less-developed nations, including China.

166 Id. at 398 (quoting unpublished GATT report: Balance of Payments Committee, Note by the Comm., Appendix and Annexes, GATT Doc. L/4200, at 14-15).
167 The Relationship, supra note 19, at 375.
1. Developed Nations and the Balance of Payments Exception

GATT's balance of payments exception stems from the era of fixed exchange rates which emerged after World War II and lasted up to the early 1970s.\(^\text{168}\) Under the Bretton Woods framework,\(^\text{169}\) the IMF achieved global exchange rate stability by requiring the developed nations to peg their currency rates to so-called "par values," which translated into a peg against gold and the U.S. dollar, or in some cases against sterling.\(^\text{170}\) This pegged rate was not supposed to shift by more than 1% in either direction.\(^\text{171}\) Thus, when a country experienced a balance of payments deficit (i.e., there was too much of its own currency in the foreign exchange market, and not enough U.S. dollars), its currency would face downward pressure. To keep the currency within 1% of its par-value, the government would have to spend its U.S. dollar holdings to mop up its excess currency in the foreign exchange market. Thus, irrespective of Article XV's requirement not to "frustrate the intent" of the charter, the GATT charter had to be flexible so that nations facing threats to their monetary reserves could restrict U.S. dollar payments on imports.

Italy, for example, adopted a mandatory surcharge on about 40% of all imports in 1974 because its central bank was running short of U.S. dollars.\(^\text{172}\) At the time, Italy needed the extra U.S. dollars earned through the surcharge in order to maintain the value of the Italian lira. Although the deposit scheme was clearly an import barrier, GATT approved it based on the Article XII balance of payments exception.\(^\text{173}\) After conferring with the IMF, GATT ruled that Italy's balance of payments situation was "exceptionally serious."\(^\text{174}\)

\(^{168}\) See Schools Brief: Managing the World's Economy, ECONOMIST, May 24, 1975, at 27-29 [hereinafter Schools Brief].
\(^{169}\) The Bretton Woods framework for international payments hinged on fixed exchange rates. It also allowed nations to borrow from the IMF under special "IMF drawing rights," and to change their exchange rates if they faced a "fundamental dis-equilibrium" in their monetary situation. \textit{Id.} at 27.
\(^{170}\) \textit{Id.}
\(^{171}\) \textit{Id.}
\(^{172}\) As of May 7, 1974, Italy required the payment of a temporary import deposit equal of 50% of the c.i.f. value (cost of goods, insurance, and freight) of the imported goods, to be paid and then held by the Italian government (with no interest accruing) for 180 days. Ultimately, GATT's Balance of Payments Committee, after conferring with the IMF, recognized that Italy's balance of payments situation was "exceptionally serious," and the measures were allowed under Art. XII. \textit{Italian Import Deposit}, GATT. Doc L-4082, BISD 21st Supp. 121, 125 (Oct. 21, 1974).
\(^{173}\) \textit{Id.} at 125.
\(^{174}\) \textit{Id.}
Article XII's balance of payments exception became largely irrelevant after the Bretton Woods par-value system broke down between 1967-1972. The Bretton Woods model proved to be unsustainable in a world of competitive exchange rates. Pressure to devalue the U.S. dollar and the British pound eventually caused a collapse of the par value system, and most currencies from developed nations were allowed to float starting from about 1972-1974. With floating rates, developed nations faced reduced pressure to maintain their currency value against an agreed upon par value.

Today Italy would have a difficult time claiming that it must impose a deposit on imports in order to shore up its monetary reserves. The reason this argument would likely fail is that the rate of the lira is no longer pegged to a par value, and thus there is no general agreement on what the rate of the lira should be. Italy can choose to devalue its currency or protect the value of its currency by investing in the currency market. It is through such intervention that a nation can protect its exchange rate and its monetary reserves.

Since the end of the par-value system, GATT discouraged nations from enacting import restrictions in order to correct a deficiency in balance of payments. With freely convertible currencies, restricting imports to shore up reserves is viewed as an inefficient option because consumers will likely shift their spending to other goods. Their overall consumption will likely not decline. For example, if a nation bans the import of sports cars to protect its balance of payments, normally this will have not have a predictable effect on consumers' ability to buy other types of imported goods. Given the availability of imports and consumer access to hard currency, trade restrictions in a developed nation have an unpredictable

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175 See generally Schools Brief, supra note 168, at 28-29.
176 Id. at 28.
177 Id. at 28-29.
178 After the era of fixed exchange rates, the major currencies were allowed to float, but not without government interventions. Most tradable currencies are weighted against baskets of other currencies, with the contents of each basket decided by the proportion of the country's trade with each other country. Id. at 29.
179 Id.
180 See Declaration on Trade Measures Taken for Balance-of-Payments Purposes, GATT Doc. L/4094, BISD 26th Supp. 205 (Nov. 28, 1979) ("Convinced that restrictive trade measures are in general an inefficient means to maintain or restore balance-of-payments equilibrium.").
181 The Relationship, supra note 19, at 375 & n.34 (quoting GATT report, International Trade 1982/83: "A change in trade barriers will alter the pattern of consumer spending, but there is no direct impact on the level of consumption.").
182 Id. at 375-76.
effect on consumer spending habits. In a world of floating exchange rates, the balance of payments exception for developed nations has thus become largely irrelevant.\(^{183}\)

2. \textit{Less-Developed Nations and the Balance of Payments Exception}

The balance of payments exception of Article XVIII(B), targeted at less-developed nations, remains a significant rule today. This article allows less-developed countries to restrict imports in order to "safeguard [their] external financial position and to ensure a level of reserves adequate for the implementation of [their] programme of economic development."\(^{184}\) This broad provision goes on to state that a less-developed nation may implement import restrictions:

(i) to forestall the imminent threat of, or to stop, a serious decline in [a member's] monetary reserves, or
(ii) in the case of a contracting party with inadequate monetary reserves, to achieve a reasonable rate of increase in its reserves.\(^{185}\)

Applying Article XVIII(B) in a fair manner has been difficult.\(^{186}\) As noted above, GATT has tried to steer all members away from adopting restrictive trade measures in order to protect monetary reserves.\(^{187}\) In 1979, GATT resolved that trade restrictions were an "inefficient means to maintain or restore balance of payments equilibrium."\(^{188}\) In other words, a nation should not restrict sportswear imports if its goal is to protect monetary reserves. In the same declaration, however, GATT noted that a less developed nation could still use import restrictions, but it would have to justify its balance of payments difficulties to GATT's Balance of Payments

\(^{183}\) Id. at 386.
\(^{184}\) GATT CHARTER art. XVIII, § B, ¶ 9.
\(^{185}\) Id.
\(^{186}\) Roessler points out that while Article XVIII(B) was meant to take into account a nation's external financial constraints, in reality many of these difficulties are structural rather than monetary. Thus, there is a strong tendency to rely on the allowable import restrictions under Article XVIII(B) to assist certain domestic sectors of a nation's economy. As a result, the protections under Article XVIII(B) tend to be invoked for a lengthy period: In late 1988, 16 out of 18 GATT members that were using Article XVIII(B) protection had been doing so for over 10 years. \textit{The Relationship}, supra note 19, at 380-81.
\(^{187}\) See Declaration on Trade Measures Taken for Balance-of-Payments Purposes, supra note 180.
\(^{188}\) Id. at 205.
Committee. The Committee, in turn, is to obtain its statistical information on the nation's balance of payments situation from the IMF, as stated in Article XV. In practice, the Committee has almost no authority to force a nation to give up its import restrictions enacted under Article XVIII(B). For example in the 1980s, at least 16 nations that had invoked Article XVIII(B) authority to limit imports had kept these measures in place for over ten years.

The 1979 GATT decision established a very lenient standard for less-developed countries. The declaration recognized outright "that the less-developed contracting parties must take into account their individual development, financial and trade situation when implementing restrictive import measures taken for balance-of-payment purposes." In other words, a less-developed nation's "individual development, financial and trade situation" may allow that nation to restrict imports in order to preserve its balance of payments.

Most critical of all is that the remedies under Article XVIII(B) are virtually non-existent for a GATT member that is affected by any Article XVIII(B) import restrictions. Article XVIII(B) does not, in principle, grant any right for an aggrieved nation to collect compensation or retaliate against a less developed member. This means that a nation invoking Article XVIII(B) may have to face ongoing consultations with the Balance of Payments Committee, but it can avoid any harsh retaliation from other GATT members.

GATT's leniency towards less developed nations does not mean that they can choose any measure to restrict imports. GATT does not want members to impose arbitrary or secret trade restrictions. Thus, the Uruguay Round modified Article XVIII(B) and the 1979 Declaration by encouraging nations with balance of payments difficulties to adopt "price-based measures," which are deemed to have the least disruptive effect on trade compared to import quotas. "Price-based measures" include import surcharges and deposit requirements such as the measure adopted by Italy in

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189 Id. at 206-8.
190 The Relationship, supra note 19, at 381.
191 Declaration on Trade Measures Taken for Balance-of-Payments Purposes, supra note 180, at 206.
192 Id.
193 The Relationship, supra note 19, at 380.
1974. These restrictions can generally be applied in an open, "transparent manner"\textsuperscript{195} to all trading partners, and thus are viewed as more fair than selective bans or quotas on certain products.

3. \textit{China's Dual-Rate Currency System Applied to the Balance of Payments Exception}

As a GATT member and a less developed nation, China’s use of a dual-rate currency probably would have been allowable under the Article XVIII(B) balance of payments exception. The key inquiry would be whether China’s monetary reserves were facing "the threat of... a serious decline," or were "inadequate."\textsuperscript{196} In either case, China could enact import restrictions to protect its reserves, although it would have to justify its choices to the Balance of Payments Committee. Under the shared jurisdiction principle of Article XV, the actual data upon which the Balance of Payments Committee would judge China’s monetary reserves situation would come from the IMF.

The problem with determining China’s monetary reserves is that the data is inconclusive. Up to 1992, China’s monetary reserves had increased but in 1993, they began to fall sharply.\textsuperscript{197} A growing trade deficit and currency outflows had drained hard currency from the People’s Bank of China and the state-run Bank of China.\textsuperscript{198} For example, China’s reserves had dropped from $46.8 billion\textsuperscript{199} at the end of 1992, to $38.2 billion\textsuperscript{200} at the beginning of 1993, a decline of 14%.\textsuperscript{201} By June 1993, China had only enough reserves to cover 4.4 months of merchandise imports, which was above the standard safety threshold of 3 months, but down sharply from earlier years.\textsuperscript{202} Moreover, many analysts believed that data on China’s

\textsuperscript{195} Id. at \S 4. "Transparent" means that the regulation is applied in a non-discriminatory matter to all parties, and does not involve any hidden costs to outsiders.
\textsuperscript{196} GATT CHARTER art. XVIII, \S B, \S 9(a)(b).
\textsuperscript{198} Id.
\textsuperscript{199} Id.
\textsuperscript{200} China’s monetary reserves are held by the central bank, the People’s Bank of China, and the state-owned Bank of China. Starting from 1992, China no longer included the monetary holdings of the Bank of China in its total reserves calculation, but the U.S. Treasury and many economists believe this is misleading since the Bank of China reserves would no doubt be available if the state needed them. \textit{See NOV. 1993 TREASURY REP., supra} note 36, at 21 & n.1.
\textsuperscript{201} Leung, \textit{supra} note 197, at 23.
\textsuperscript{202} Id.
balance of payments account did not accurately reflect the problem of short-term capital outflows.203

Given the uncertain data on China, it would be difficult for GATT or the IMF to ascertain the severity of China’s balance of payments situation if a trade complaint arose under Article XV. For example, the growing complexity in the linkages between China, Hong Kong, and foreign investors has obscured how much money is flowing in and out of China.204 Signs of this are apparent in China’s statistical reporting. Between the first half and the second half of 1992, the category of “errors and omissions” in China’s balance of payments account more than doubled (from $5.8 to $12.2 billion), likely reflecting a large increase in short-term capital outflows.205

What probably worried GATT members during the Uruguay Round is that China, as a member, would have qualified for the Article XVIII(B)(9) balance of payments exception based on its 1993 decrease in monetary reserves and the uncertain data. China could have argued that the 14% drop in reserves qualified as a “threat,” and thus China was justified to enact import restrictions to forestall a further decline. China might also have benefited from the overall uncertainty of the data, depending on which information the Balance of Payments Committee decided to consider, and how heavily it weighed such information. At least some observers believed that by the end of 1992, China was recording net capital outflows, instead of inflows as indicated by China’s official statistics.206

203 Many economists agree that China’s capital movements are not accurately reflected in China’s official statistics. Peter Harrold and Rajiv Lall, writing for the World Bank, contend that short-term capital outflows are not accounted for in China’s data. In large part this is due to the growing number of foreign subsidiaries of Chinese firms and the increasing numbers of “legal and illegal channels for funds to move in and out of China.” Harrold & Lall, supra note 76, at 14. The Wall St. Journal has editorialized on the nature of these legal and illegal channels. Noting that estimates of China’s hidden capital outflows in 1992, range from US$ 8 billion to US$ 20 billion, The Wall St. Journal pointed a finger at official corruption:

[It]’s safe to assume that much of the outflow represents the illegal gains of well-connected Chinese officials. Nobody doubts that turning state assets into private riches has become the primary occupation of the families of party bigwigs. For all we know, though, these illicit riches are making a round trip, dipping offshore just long enough to disguise ownership and qualify for the tax advantages due foreign investors and joint-venturers.

Lenders can hardly be so confident that the billions loaned directly to Beijing aren’t being squandered or salted away. Nor can the share investors now being courted to become Beijing’s partners in dozens of state enterprises discount the possibility that their funds will end up in the regime’s retirement accounts rather than paying to upgrade production and return them a profit.


204 Harrold & Lall, supra note 76, at 14.

205 Id.

206 Id.
Assuming China could qualify for the balance of payments exception under Article XVIII(B), the second question would have been whether the measures China adopted to restrict imports (i.e., restricting access to the swap centers) were valid under GATT rules. Recall that the swap centers restricted imports by denying access to foreign exchange. A GATT member could have certainly argued that these import restrictions were not enforced in a "transparent" manner, since they were not applied evenly to all nations. Also, the rules governing currency transactions were often so broad that officials could use their discretion to deny access if they wanted.

However, China's method of restricting imports is a detail in the context of an Article XVIII(B) dispute. For GATT members, the real worry was that China could minimally qualify for the balance of payments exception. Since Article XVIII(B) affords no opportunity for retaliation, if China qualified for this exception then the worst it would face would be a series of consultations with the Balance of Payments Committee. In effect, once China qualified under Article XVIII(B), the Balance of Payments Committee could do little more than question China and provide advice on alternative measures.

In an Article XVIII(B) dispute, GATT could try to steer China towards adopting some kind of across-the-board pricing measure, such as a surcharge on imports. But China, as a less-developed nation, could make a strong case for leniency. As the 1979 resolution states, a less-developed nation may take into account its "individual development, financial, and trade situation" in deciding which type of trade restrictions to impose. China could argue that given its former import substitution policies and overvalued currency, a dual-rate regime was an essential step in integrating its economy with the outside world. China could ask for more time to overhaul its currency structure. China might have succeeded, especially if the IMF and the data was supportive. On balance, the factors to be weighed seemed to favor lenient treatment for China. Thus, the working party sought to delay China's membership.

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207 See Understanding on the Balance-Of-Payments Provisions of the General Agreement on Tariffs and Trade ¶ 4, supra note 194, at 1 (requiring that import restrictions taken for balance of payments reasons "shall be administered in a transparent manner").


209 Declaration on Trade Measures Taken for Balance-Of-Payments Purposes, supra note 180, at 206.
IV. POST-URUGUAY STRATEGIES FOR CHINA AND GATT

A. Background on the Close of the Uruguay Round

The Uruguay Round ended with two conclusions reached regarding China's accession. First, the working party decided that China was not yet ready to accede to GATT. Second, China's dual-rate currency mechanism had become one of the key obstacles to China's bid. Interestingly, after the Uruguay Round closed, even China agreed that it would have to unify its exchange rates to join GATT. The parties had indeed reached some common ground on the need of exchange rate reform.

Each party working on China's bid (the GATT working party, the U.S., and Beijing) had its own reasons for favoring currency reform. Their reasons stemmed from the inapplicability of the GATT-IMF framework against China's currency practices. In the end, China was deemed not ready to join GATT, but China hoped to do so once it unified its exchange rates.

The question remains whether Beijing's currency reforms implemented on January 1, 1994, will be enough to ensure China's membership to GATT.

B. China Announces a Unified Exchange Rate

At the end of 1993, China announced that it would unify its official rate and the swap center rate as of January 1, 1994. This surprise decision presents a new dimension to the GATT talks. Although the Uruguay Round had already ended when China made the announcement, China will continue meeting with the GATT working party in Geneva, and hopes to be admitted to the trade body by early 1995, in time for the WTO. In

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210 See Talks on China's GATT Membership End, supra note 40, at 490.
211 See New Foreign Exchange Rate, supra note 41.
212 Id.
214 Id.
215 China would like to be a member of GATT so that it can be a founding member of the World Trade Organization, which will succeed GATT in 1995. Frances Williams, GATT Members Warm to China's Entry, FIN. TIMES (London), Mar. 16, 1994, at 7.
China’s view, the single rate structure now in place should put to rest the GATT’s concern about exchange rate matters.\textsuperscript{216}

China’s new currency mechanism eliminates the dual-rate structure and replaces it with a single rate. However, it is unclear to what extent the new system will avoid the problems of the swap centers, such as arbitrary access to foreign exchange and hidden regulations. On January 1, 1994, the new unified exchange rate was set at 8.7 yuan per dollar, in line with the former swap center rate. In effect, the former official rate of 5.7 was devalued about 52% to reach the new unified rate. Perhaps the most important point of the currency reforms is that the former retention system, which allowed certain enterprises to keep 50% of their foreign exchange earnings, was eliminated. In its place, China has created an inter-bank foreign exchange market, where domestic enterprises are allowed to acquire hard currency as long as they have the proper import licenses.\textsuperscript{217}

The workings of China’s new foreign exchange rules remain unclear. According to China’s public statements, most non-business enterprises and individuals will be allowed to have foreign currency accounts,\textsuperscript{218} as will some investment and holding enterprises.\textsuperscript{219} Foreign-invested companies likewise will have foreign exchange cash accounts, but it is unclear whether they will be able to acquire hard currency at Chinese banks.\textsuperscript{220} The swap centers apparently remain in place for the purpose of serving foreign companies.\textsuperscript{221} Thus, the government seems to be sensitive to the currency needs of foreign investors, and does not want to change the former system too quickly. However, there are also indications that Chinese banks continue to

\textsuperscript{216} Wu Yi, minister of foreign trade and economic co-operation, was quoted on Dec. 29, 1993, as saying: "The adoption of a new single floating exchange rate from January 1, 1994, will help bring China's foreign trade operations closer to the international norms and play a positive role in resuming China's signatory status in the General Agreement on Tariffs and Trade." See New Foreign Exchange Rate, supra note 41.

\textsuperscript{217} See Note on New Foreign Exchange System, supra note 213.

\textsuperscript{218} Diplomatic missions, offices of international organizations, "and other non-resident legal entities in China" will be allowed to have foreign currency accounts. Id.

\textsuperscript{219} Foreign currency accounts will be allowed for: "remittance(s) for the purpose of investments by any nonresident legal entities and natural persons, ... external borrowing, ... funds remitted back to China by the service contract companies within the contract period of their overseas projects for current use of the project, [and] receipts from foreign donations and grants." Id.

\textsuperscript{220} "If, for the purpose of production, operation, debts service, and profit remittance, they need more foreign exchange after being authorized by the foreign exchange administrative departments according to relevant regulations, these enterprises can also purchase foreign exchange from the designated banks." Id.

\textsuperscript{221} Carl Goldstein, A Lighter Shade of Red, FAR EASTERN ECON. REV., Apr. 28, 1994, at 79.
restrict access to foreign exchange requests made by domestic companies.

After several months of delay, China finally opened a national exchange center in Shanghai on April 4, 1994, to exchange U.S. dollars, Hong Kong dollars, and yuan. The Shanghai center is to be the hub of China's inter-bank exchange market. It links to trading centers in Beijing, Tianjin, Hangzhou, Shenzhen, and Guangzhou. Altogether, thirteen domestic banks and over eighty other Chinese and foreign banks and non bank financial institutions will interact with the Shanghai market. Although the inter-bank market draws in money traders from throughout the country, the government will apparently keep the yuan rate tightly controlled.

For GATT members, the key inquiry is how China chooses to limit expenditures of foreign exchange under this inter-bank system. Recall that dual currency rates are against GATT principles because: (1) they allow nations to arbitrarily subsidize certain industries; and (2) through administrative measures, dual currency rates are easily parlayed into an additional level of import barrier. The working party handling China's bid might be convinced that China's unitary rate has solved the first problem. With a single rate, China's exchange rate practices will no longer subsidize certain sectors by allowing them to buy and sell foreign exchange at the most favorable price. Thus, the former system of cross-subsidies, at least as they were applied through China's dual-rate regime, is perhaps no longer a worry. However, the second problem is far from solved. The working party has a right to scrutinize how the new inter-bank market will be administered. The working party should ask for proof that the inter-bank market will allow fair access to foreign exchange, based on rules that are known by all buyers.

Regardless of China's public confidence that its currency reform will vault it into GATT, it is unclear that Beijing has solved the problem of arbitrariness with respect to who gets access to foreign exchange.

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222 Id.
224 On the first day of trading at the Shanghai market, the U.S. dollar opened at 8.681 yuan and traded within a very narrow range: between 8.7265 and 8.681 yuan, or about .5% above the opening rate. Trading closed at 8.6908 yuan. Id.
225 China outwardly recognizes that standardized rules on foreign exchange transactions are an essential requirement: "Rules and regulations will be made to normalize and legalize the foreign exchange trading so that the regulation and supervision can be conducted with a sound legal base." Id.
Administrators of the Shanghai market, for example, may be granted discretion to curtail trading or reject requests for exchanges just as the swap centers used to do. Only time will answer this question.

Ultimately, the working party should be careful not to judge China’s new currency mechanism in isolation, but should instead ask how the effects of China’s new inter-bank market might be nullified through other measures. Consider, for example, China’s announcement on January 1, that it will restrict imports on machinery and electronics in 1994.\textsuperscript{226} China emphasized that these new restrictions would be implemented in the form of quotas, but once again this points out that the definition of “quota” is a slippery one. To China, a quota on the import of machinery and electronics might mean a quota \textit{in effect} (i.e., that banks in the inter-bank market will arbitrarily decide which enterprises have access to foreign exchange in order to import machinery and electronics). As noted above, this sort of restriction might still be defensible under GATT’s Article XVIII(B) balance of payments exception, assuming China’s monetary reserves are at risk, but at minimum it would require open publication of the quota and consultation with GATT’s Balance of Payments Committee.

C. \textit{Renewed Attention Needed on the Issue of Transparency}

The debate concerning quotas versus currency controls will continue in the GATT talks, but at least one obstacle for China has become clear: GATT members’ criticism of China’s former dual-rate currency system is mainly based on how China administered that system through internal regulations. The negotiations on China have involved exhaustive fact-finding on exactly how China operates its economy.\textsuperscript{227} With respect to the swap centers, the rules were neither public nor transparent, allowing officials to easily limit access to hard currency.\textsuperscript{228} The rules that China published regarding its swap centers allowed for broad discretion in rejecting currency exchange requests, which in effect allowed officials to enforce on-the-spot trade barriers.

In the ongoing talks between China and GATT, the working party should not ignore Article X of GATT, which requires open publication of

\begin{footnotesize}
\begin{enumerate}
\item[227] See supra note 15.
\item[228] Nov. 1993 TREASURY REP., supra note 36, at 24.
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all laws and regulations that affect trade. A fair question is whether China intends to honor this Article under its new unitary currency regime. For example, in the case of restrictions on electronics and machinery imports, will China’s trading partners be alerted as to which electronics and equipment are affected, or will the quotas act as “secret quotas,” as the U.S. has charged? Unless China can answer these questions, China should not be allowed into GATT. Given China’s track record of using currency measures as import quotas, and the ineffectiveness of the GATT-IMF framework with respect to currency issues, the working party should not simply cave in to China simply because the WTO is under formation. Instead, the working party should ask for a review period of at least a year so that China’s new inter-bank market can be studied in operation. The “secret quotas” issue is indeed a real concern.

D. Protocol of Accession

It is difficult to predict whether China will be admitted to GATT or the WTO. If admitted, however, GATT must decide on what concessions to require. The accession process to GATT requires a negotiation process followed by a protocol stating the terms under which accession is granted. The protocol must include a detailed schedule of tariff reductions that the country agrees to follow. In China’s case, the working party did not begin the task of drafting its accession protocol during the Uruguay Round. The working party handling China’s application continued to hold talks with China after the Uruguay Round. On March 16, 1994, the working party met to hear China outline its blueprint for continued reform. Among the promises, China pledged to liberalize import restrictions on over 500 tariff lines, make licensing and quotas more transparent, and once admitted to GATT, to phase out 80% of existing non-tariff measures by 2000 and make the yuan fully convertible by 2000. China’s performance was generally welcomed, but the U.S. Trade Representative delegate said that the U.S. “cannot subscribe to an artificial deadline” on China’s application, and that the U.S. still had a long list of questions for China. See Working Party on China Reconvenes; U.S. Will Not Commit to Firm Timetable, 11 INT’L TRADE REP. (BNA) 419 (Mar. 16, 1994).

229 Article X clearly prohibits the use of unpublished restrictions, regardless of whether the restrictions are “monetary” or “trade” in character: “No measure . . . imposing a new or more burdensome requirement, restriction or prohibition on imports, or on the transfer of payments therefor, shall be enforced before such measure has been officially published.” GATT CHARTER art. X, ¶ 2.

230 See U.S. Not Ready to Back China’s Accession to New World Trade Group, Official Says, 11 INT’L TRADE REP. (BNA) 617 (Apr. 20, 1994) (quoting an anonymous U.S. trade official as saying the U.S. was reluctant to support China’s bid to join the WTO: “We don’t see how a WTO can have secret quotas. There can’t be secrets among WTO members about their import regimes. They have to be public; they have to be transparent.”).

231 Accession is provided for under Article XXXIII. GATT CHARTER art. XXXIII.
If China is deemed fit to enter GATT, the drafting of the accession document gives GATT members an opportunity to require periodic review of China's currency practices.

The accession protocol offers GATT members a chance to solidify their negotiations into a series of rules and procedural instructions. For most countries, the accession document is straightforward. For example, the accession protocols for the Philippines and Columbia are 2-3 pages each, and contain few specifics aside from the tariff schedules. On the other hand, the formerly communist countries, such as Poland, Hungary, and Romania, agreed to more detailed protocols. At minimum, China's accession document should follow the example of the former East European countries. Many trade analysts have drawn parallels between the accession of the East Bloc countries and the case of China, but they are quick to note that China presents a unique situation due to its size and economic differences.

Nonetheless, the precedents of Poland, Hungary, and Romania could be useful in terms of procedural requirements. In the protocols of accession of all three eastern European nations GATT took the extraordinary step of including special requirements related to foreign exchange. At the time, Poland, Hungary, and Romania were not members of the IMF, so the Balance of Payments Committee could not rely on IMF-supplied information under Article XV. However, all three nations agreed that they would

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233 In 1992, several developing nations represented in the working party supported the early drafting of an accession protocol for China, but they were blocked by the U.S., the E.C., and other Western nations. See U.S., EC Balk At Immediate Drafting of GATT Accession Protocol for China, 9 INT'L TRADE REP. (BNA) 313 (Feb. 19, 1992).

234 Under Article XXXIII, accession is made based on "terms to be agreed between [the acceding nation] and the CONTRACTING PARTIES." GATT CHARTER art. XXXIII. Some GATT entrants (including Switzerland, Thailand, the Philippines, Hungary, Romania, and Poland) have acceded under protocols of accession that specifically except them from various GATT provisions. See GATT, Analytical Index, art. XXXIII, ¶ 8 (1989).


239 Protocol for the Accession of Romania to the General Agreement on Tariffs and Trade, BISD 18th Supp. 5 (Oct. 15, 1971).


241 See GATT CHARTER art. XV, ¶ 2-6.
follow "the intent of the General Agreement" with respect to exchange matters, and also agreed to consult fully with the Contracting Parties if any GATT member thought their currency system was violating the GATT charter. The accession documents added an oversight mechanism: If GATT members found that Poland, Hungary, or Romania took measures not in accord with GATT principles, then the country would be required to enter into a "special exchange arrangement" with the Contracting Parties, as provided for under Article XV(6).

An important detail in the accession protocols of the three East European nations was the required surveillance process. All three countries were obligated to submit to annual reviews of their performance within GATT. Included in these reviews was an examination of their balance of payments situation, and whether their balance of payments warranted restrictions on imports. These annual reviews did not bring about strict policing of currency measures, but at minimum they brought the balance of payments question under an agreed-to framework for oversight. In this way, the accession protocols set up a system for applying normative pressure.

In the annual reviews, all three nations were required to provide up-to-date information on their monetary situations, and complaints were filed in several cases when this requirement was not met. For example, Poland faced pressure in its sixth and ninth annual reviews for not providing detailed information on its balance of payments situation. Romania faced similar concern in its second review. Of course, members of the public are not privy to these annual reviews, and both Poland and Romania fended

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242 See BISD 15th Suppl., supra note 237, at 49; BISD 20th Suppl, supra note 238, at 6; BISD 18th Suppl., supra note 239, at 8.
243 A "special exchange agreement" with GATT would require the country to uphold agreed-to rules regarding foreign exchange, and would become part of the country's obligations under GATT. GATT CHARTER art. XV, ¶ 6.
244 BISD, supra notes 237-39.
246 GATT members apparently continued to prod Poland to provide better information on "errors and omissions," capital movements allocated to trade versus capital movements allocated to "economic cooperation" with other (East Bloc) nations, and activities of the central monetary authorities. Consultation with Poland: Ninth Review Under the Protocol of Accession, GATT Doc. L/4483, BISD 24th Suppl. 139, 148 (May 23, 1977).
247 Romania's balance of payments data were said to be deficient for not showing "invisibles and long-term credit operations." Consultation with Romania: Second Review Under the Protocol of Accession, GATT Doc. L/4469, BISD 24th Supp. 149, 152 (Mar. 2, 1977).
off the pressure in these meetings. But the mere fact that these reviews took place periodically, and that some attention was paid to currency and information access, should be enough to interest those in charge of drafting China's accession protocol.

Given the leniency that GATT affords to less-developed nations, GATT is not really able to force these members to adopt certain policies. However, GATT's review process continues to be an important tool in persuading nations to adopt limited import barriers and in making these barriers widely-known. In 1991, for example, the Balance of Payments Committee oversaw an import surcharge scheme put in place by the Czech and Slovak Federal Republic, and noted that this surcharge had been reduced and was intended to be abolished by the end of 1991.248 The Committee also notified Turkey that it would face a full consultation regarding its import restrictions taken for balance of payments purposes,249 and warned the Philippines to notify GATT regarding its 9% import surcharge.250

Continued scrutiny of China's trade policies would be critical if China was admitted to GATT. If the Uruguay Round proved anything it is that holding China's trade regime up to international scrutiny has an inherent value. In particular, the process brought about a heightened understanding of China's actual trade practices. It is not an understatement to say that this knowledge would probably not have come about through any other means. The former dual-rate regime was so riddled with arbitrary decision-making and internal procedures that it is unlikely observers could have understood its workings simply by reading China's currency laws. Moreover, GATT's multilateral forums served to bring unified pressure against China's currency practices. A body like GATT was able to penetrate China's currency regime by asking questions over seven years, and ultimately by withholding China's entry pending a currency reform. This process of question and response should not stop simply because China adopts a unitary rate. Nor should it stop if China is allowed to accede to GATT.

Many GATT members are asking for China's accession protocol to include a safeguard clause, whereby any nation suffering from a flood of

249 Id. at 13.
250 Id.
Chinese goods could elect to unilaterally limit Chinese imports. This measure provides a big stick for countries to retaliate against China should China dump its goods overseas. Not surprisingly, it has gained considerable support. But ultimately the safeguard clause is a measure that attaches to China's imports. As for opening China's market, this will only come about through positive steps on the part of China. Consistent pressure from GATT is important. One way to apply such pressure is to ensure that China faces continued scrutiny regarding its restrictions on foreign exchange access. This approach will safeguard the principle inherent in Article X: namely, that China cannot rely on secret rules. If China is deemed fit to enter GATT, the working parties should be careful to include a process of annual review in China's protocol of accession.

V. Conclusion

China's former dual-rate currency mechanism raised many trade questions for the U.S. and the working party handling China's application to join GATT. The dual-rate structure enabled China to subsidize certain industries, and acted as a mechanism to tax foreign exchange transactions and limit imports. Pressure to scrap the dual-rate structure built up during the Uruguay Round of GATT talks, and ultimately China agreed to adopt a unitary exchange rate shortly after the Uruguay Round ended.

Troubling aspects of China's unitary exchange rate, adopted in 1994, are the problems of information access and fair enforcement. China still faces many questions, including these: Will China continue to use currency measures to limit imports? Will China be able to undermine the concessions it offers to GATT (such as tariff cuts) by erecting administrative barriers to hard currency access? If China's monetary reserves slide, will GATT's Balance of Payments Committee be able to steer China away from import quotas and towards "price-based measures," as was resolved in the Uruguay Round? These are fundamental questions that must still be answered even under China's unitary exchange rate. Before China enters GATT, at minimum GATT members should observe China's new unitary rate and its inter-bank exchange market. A waiting period of at least a year would be reasonable, during which time China should not be admitted to GATT but should be willing to answer questions.

251 See China Agrees to Accept Conditions on Re-entry in GATT, Brittan Says, 11 INT'L TRADE REP. (BNA) 384 (Mar. 9, 1994).
If China can convince the working party that it is deserving of GATT membership, and receive the needed two thirds vote from GATT members for entry, then the Contracting Parties should be careful to commit China to a series of annual reviews regarding balance of payments and information access. Such a schedule for review should be outlined in the protocol of accession. Careful drafting of this protocol is important because the GATT-IMF framework offers few legal controls in the area of currency controls. The main value of the GATT-IMF framework is procedural; Article XV of GATT provides for a multilateral forum to examine a member's import restrictions taken to protect monetary reserves. China should not be allowed to evade this process. GATT members should recognize that even if China is admitted to the organization, the fact-finding process on China's trade regime has only just begun.