

RECONCILIATION OF NON-MARKET ECONOMIES:

GATT TRADE RULES

By

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ABSTRACT

Due to the abortion of the proposed Havana Charter and non-participation of the USSR and other State trading economies in the Charter negotiations, GATT has been acting as a traders' club - a club mainly beneficial to western market economies. Its rules are formulated almost exclusively in favor of free trade on a comparative advantage and private enterprise basis. There is virtually no place for NMEs to have effective access. As one of the pivots of post-World-War-II multilateralism, GATT assumes a major role in compromising, integrating, regulating and supervising diversified member nations' trade laws and policies. Its legal framework, however, is inadequate to deal with the integration of NME. This is because GATT is framed essentially along the line of market ideology and minimal government intervention. NMEs, on the other hand, discard market ideology and adopt wholesale government intervention and central planning as a basic form of economy.

While trading practice in NMEs is basically incompatible with the GATT-promoted free trade rules, accommodations were made to facilitate NMEs' request for membership. Consequently, Poland, Romania, Hungary and Yugoslavia became GATT members respectively during the 1960s and 70s. At that time East European countries maintained command state trading thus were unable to be fully

integrated into the GATT-based international trade order. During negotiations on terms of NMEs' accession to GATT, GATT countries adopted an import commitments approach to solve the central and much debated issue of market access to NME countries. Despite its merits, the approach has been criticized notwithstanding the fact that no alternative has been suggested.

Accordingly, the primary objective of the thesis is to rethink the existing approaches to NMEs in order to explore new ways of effectively integrating NMEs into the GATT legal framework. By approaching the thesis problem carefully, the writer arrives at the conclusion that although GATT would need new assumptions with a view to regaining a new consensus of broader international representation and participation, a considerable and substantial decentralization in the NME is unavoidable in order to adapt themselves into the GATT framework. In the meantime, it is stressed that all GATT countries should continue to facilitate NMEs' access to the GATT forum in the hope that NMEs being potential world traders would increase world prosperity and understanding by broader participation. World prosperity, needless to say, is the best guarantee of world peace and security.

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LIST OF ABBREVIATIONS

c.i.f.--cost, insurance and freight

CMEA--Council for Mutual Economic Aid, also referred to as

COMECON

CPs(cps)--Contracting Parties

ECSC--European Council of Steel and Coals

EEC--European Economic Community

EFTA--European Free Trade Association

f.o.b.--free-on-board

FMEs--free-market economies

GATT--General Agreement on Tariffs and Trade

GSPs--Generalized Special Preferences

IMF--International Monetary Fund

ITO--International Trade Organization

LDCs--less-developed countries

MFN--most-favored-nation

MTN--Multinational Trade Negotiations

NMEs--non-market economies

NTBs--non-tariff barriers

OECD--Organization for Economic Cooperation and Development

OPEC--Organization of Petroleum Exporting Countries

QRs--quantitative restrictions

SDRs--Special Drawing Rights

STEs--state trading enterprises

UN--United Nations

UNCTAD--United Nations Conferences on Trade and Development

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While many ardent scholars and writers have brought distinguished credentials to the discipline of the General Agreement on Tariffs and Trade (GATT), there is yet a gap left for us to fill in the relationship between the GATT trading system and nonmarket economies (NMEs). The primary objective of the thesis is to fill this gap.

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On my final note I should add that I am solely responsible for the facts and opinions set out in this thesis.

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P A R T O N E : I N T R O D U C T I O N

1. THESIS PROBLEMS: MAIN THEME OF THE THESIS

The thesis centers on the issue of reconciliation of market-based GATT legal framework with non-market economies (hereinafter "NME"). The purpose of the thesis is first to examine whether the NME system is compatible with the GATT trade rules. As GATT rules are almost exclusively formulated along the pattern of market economy ideology which is in constant conflict with the centrally planned socialist system, the effectiveness of NME countries' access to GATT is doubtful, and the ability of NMEs to meet the GATT code of conduct in trade is rather limited. Because GATT is essentially created on the principle of freer trade and non-discrimination for market economies particularly private-enterprise economies, it is unlikely to provide an adequate framework to deal with NMEs and particularly state-trading economies. In view of this problem the thesis undertakes to explore some feasible and rational mechanisms that will accommodate NMEs to participate in the GATT.

GATT solved the problem of the accession of East European countries to membership on a country-by-country and very pragmatic basis. The GATT pragmatism is obvious by using an import-commitment-oriented approach to solve reciprocal

market-access issues putting aside its cardinal principle of non-discrimination. The requests of China and even the USSR for GATT membership pose new challenges to trade liberalization and integration within the ambit of the GATT. Some unsolved theoretical and structural problems pertaining to the compatibility and reconcilability of the NME and GATT rules must be examined and considered.

The study is also designed to deepen understanding of the GATT legal framework, to reconcile the incompatibility of NME with GATT trade rules, to propose possible solutions to integration of NMEs into GATT legal regime.

2. THESIS ORGANIZATION AND ANALYSIS

The thesis consists of three parts besides the introduction (Part I) and the conclusion (Part V). As its dominant theme revolves around the reconciliation of NME state-trading system and GATT framework, Part II of the thesis begins by setting out the ideological, historical and philosophical background for the establishment of the GATT system and the exclusion of NME countries from GATT membership. This part is crucial because it illustrates basic theories, assumptions and doctrines on which the GATT multilateralism was framed. It will provide readers with a better sense of how and in what context the GATT rules were negotiated and formulated.

It then states the economic and political theory upon which GATT is based and outlines Marxist economic theory dominating almost every socialist country and how or why the theory has been modified by the Eastern bloc and China.

Part III of the thesis examines some major areas which would raise the issue of compatibility between the function of non-market state-trading economies and GATT rules. To this end, the thesis undertakes a rule-by-rule approach, as opposed to a "linear approach" employed in part I, to analyze selected GATT principles or rules and their applicability to non-market economies. Principles of non-discrimination, reciprocity, tariff protection, and rules and requirements concerning state-trading, use of protectionist mechanisms for the purpose of trade controls including the use of quantitative restrictions (QRs) are examined. It is believed that by using this approach the question of the compatibility and reconcilability of the NME and GATT trade rules could be better answered and be made clearer. Since non-market economies are essentially state-trading,¹ the focus of this analysis is on state trading systems in major NMEs, namely, China, the USSR and the Eastern European countries. Mexico, and some other OPEC state trading countries are excluded due to the limited resources of those countries and the confined scope of the study.

Part IV of the thesis proposes certain mechanisms desirable for the integration and reconciliation taking into account GATT's previous experience with integrating the

Eastern bloc into the GATT. Since the most immediate concern of GATT is with China's membership request, a portion of this part will be devoted to discussing the compatibility of China's economy with GATT and exploring options for China's accession.

In establishing a reconciliation mechanism, this part of the thesis also undertakes to review the GATT approaches towards accepting Eastern European countries into its framework. It also reviews the GATT experiences in dealing with some apparently irreconcilable problems at the time of some East European NMEs' accession to GATT. With these approaches and experiences as guidance, the thesis then particularizes the problems concerning China's accession or resumption.²

The thesis concludes with a summary of the study and assessment of GATT's role in integrating the NMEs into its regulatory framework.

3. THESIS METHODOLOGY

Traditional approaches to academic theses are devoted more to philosophical or doctrinal analysis. Today, many scholars are more inclined to be problem-solving theorists. The overriding methodology of this study is a problem-solving approach which requires a deductive and inductive reasoning, a multi-dimensional analysis of theory and current practice, a comparative study with a combination of descriptive,

analytical, imaginative and presupposed mechanics. As compared to a traditional philosophical or doctrinal approach, the problem-solving approach may have more practical significance. It concentrates more on particular problems and aims at practical application. There is, however, a danger in this approach that will undermine the creativity of the study. Such an approach may meet the utility and novelty requirements but may lack provocative ideas, which are essential to advance a general field.

Like any other research, this study begins by laying down preliminary assumptions. Efforts have been made to analyze, justify, and establish the assumptions. Thesis arguments will hopefully be evidenced and supported in the course of analysis, though they would remain debatable in changed circumstances. Admittedly some of the subject contentious issues might remain unsolved and others might have several solutions. Conclusions of the thesis thus may appear open-ended. This is especially so because the two major NMEs-China and the Soviet Union-have not yet acquired GATT membership. This would render it hardly predictable as to how GATT member countries are to integrate them into GATT's framework and what terms of accession need to be negotiated.

4. OPTIONS AND PRELIMINARY CONCLUSION

As regards the integration of East and West trading systems, one of the most frustrating and much discussed

problems is State trading.³ State trading exists in both market and non-market economies. State trading remains a notable barrier to trade, a tough trade instrument which is at odds with GATT-promoted trade liberalization. To a large degree GATT rules on state trading have not become an efficient instrument in dealing with state trading problem. Revision of some GATT rules is believed to be both crucial and demanding with a view to reconciling NMEs with GATT. Economic analysis of state trading system shows that state trading can be both an object of trade policy and instrument of trade policy.

Traditionally, GATT attached too much weight to defining state trading enterprises (STEs) themselves. It neglected the function of government control behind the activities of STEs. It is thus submitted that GATT, with an objective of decentralizing state trading system, should focus on regulating state trading as an implementation of government trade policy rather than on STEs per se. Some of previous GATT approaches to NME's state trading such as "normative approach"⁴, "result-oriented approach"⁵ or "import commitment approach"⁶ dealt with "on a country-by-country basis"⁷ might no longer be appropriate. Some rethinking of those approaches would be conducive to identifying the problems and would offer us some workable options for re-integrating today's diversifying trade systems.

However, the review of the GATT approaches (normative approach, result-oriented approach or import commitment

approach and country-by-country approach) would show that to integrate the NME into the GATT system is by no means an easy task. It would be simply irreconcilable if neither the NME system nor the original GATT assumptions on which the GATT rules were based were to be changed. In addressing this reconciliation issue the GATT countries should continue to be realistic otherwise the goal of reconciliation would not be attained. To reconcile the NME with the GATT framework or the GATT with the NME system, the following four options merit consideration:

Option I: Either NMEs reform their economies and foreign trade regimes to such a degree that their economies are compatible enough with the GATT system and follow GATT trade rules as though they were market economies, or

Option II: Regardless of its deep-rooted trade liberalization notion with the function of market force, GATT should revise and insert relevant articles dealing with NMEs' state trading along the lines suggested in the U.S. "Suggested Charter" for the founding of the International Trade Organization (ITO) at the London Conference,⁸ or "the Havana Charter"⁹ to recognize state trading as an instrument of trade control and to use "effects of material injury"¹⁰ approach to overcome the dilemma with the state trading problem, or

Option III: Integrating NMEs, China and the USSR in particular, into the GATT framework on the basis of special arrangements. Basically this is a country-by-country approach

by which the Eastern European bloc has formerly been integrated, or

Option IV: NMEs give up any attempt to join the GATT because of their inability or unwillingness to completely accept the market-based GATT forum - a forum which is labelled a "rich men's club".

The above proposals are illustrative but by no means exhaustive. There may exist other options which will hopefully be mentioned in course of discussion. The focal point of the option analysis is to see in the final analysis which option is most appropriate to solve the problem of integrating state trading systems into GATT legal regime.

FOOTNOTES

- 1 State trading, as compared to private trading, denotes a trading system where the volume and prices of a country's exports and imports are pre-determined by the state. Foreign trade is apparently an exclusive domain of government regulation. See K.W. Dam, *The GATT Law and International Economic Organization* (1970), concerning "state trading", pp. 316-31.
- 2 China was once the original member of the GATT. In 1958 the Nationalist Government in Taiwan withdrew its membership from the GATT due to economic factors. In spite of the nationalists' withdrawal, PRC's Beijing Government declares that it was invalid simply because only Beijing government is the legal representative of China. This claim is consistent with the view expressed in resuming China's seats in the United Nations, the International Monetary Fund and the World Bank institution. See Li, Chungzhou "Resumption of China's GATT Membership" (1987) 21 *J.W.T.L.*, pp.25-48.

- 3 State trading refers to trading planned and targeted by the State rather than by private enterprises (see *supra* note 1). The following is M. Kostecky's definition of state trading: "State trading occurs when a government or a government-backed agency determines the essential terms (including prices or quantities) on which exports and imports have to take place." Regardless of the significance of public ownership, government management, public grant of exclusive rights or state monopoly of foreign trade, Kostecky adopts a functional approach to define state trading as one of many methods of government intervention in foreign trade. See Kostecky, "State Trading By the Advanced and Developing Countries: The Background," in *STATE TRADING IN INTERNATIONAL MARKETS* (1982, Kostecky ed.), at 6-8. The functional approach perhaps provides the best starting point for later discussions in Part III of the dissertation since state trading is in terms of foreign trade at the heart of non-market economy.
- 4 Under "normative approach", the GATT declares that the parties must not induce or tolerate practices of state trading enterprises that have effects which would be violation of commitments under the General Agreement. Roessler, "State Trading and Trade Liberalization", in *STATE TRADING IN INTERNATIONAL MARKETS* (1982 Kostecky, ed.), at 275. Viewing GATT from a normative angle, the author distinguishes **rules** from **measures** (a rule, being addressed to an unknown number of enterprises, necessarily has to be made public before it can become effective, a measure, however, being addressed to one or several specific enterprises, need not be made public). This rule-oriented approach of the GATT is not an efficient instrument to prevent specific government measures of a discriminatory or protective nature, made effective through state-controlled enterprises. For detailed discussion of the drawbacks of the approach, see Roessler, *id.*, at 261, 263, 275-76.
- 5 This approach provides for commitments to achieve agreed targets through state trading enterprises. It was first used by France. (See GATT Consolidated Schedules of Tariff Concessions, Vol. 2 Geneva: 1952, p. 200.) and later overused when dealing with Polish and Romanian problems of accession to GATT. It is basically synonymous with "import commitment approach". See Roessler, *supra* note 4, at 262, 276.

- 6 Import commitment approach is such that the basis of admission was to be provided not by tariff concessions but by a commitment to achieve a minimal volume of imports from the GATT countries. For instance the Polish Protocol of Accession set the annual increase of imports from the GATT members at 7%. (GATT Doc. L/2851 July 1976). The Protocol of Accession with Romania in 1967 stated that Romania intends "...to increase its imports from the contracting parties as a whole at a rate not smaller than the growth of total Romanian imports provided in its Five Year Plan." (GATT Doc. L/3557, Accession of Romania 5 Aug. 1971, 807 UNTS 312).
- 7 A "country by country approach" became necessary when Eastern European countries were applying for the GATT membership not simultaneously and each had more or less different state trading system. Some of them adopted "command" or directive state trading system; some used relatively "loose" state trading system. See Kostecki, *East-West Trade and the GATT System* (1978), pp. 46-51. Kostecki attacked this approach because it could not solve the ultimate problem of integrating the NME countries into the GATT framework, but he failed to provide a better substitute. In view of this another writer tends to choose "Part V approach", i.e. adding Part V which exclusively deals with NMEs to the original text of the GATT, to solve the problem. See E. Patterson, "Improving GATT Rules for NMEs", 20 *J.W.T.L.* 185 (1986).
- 8 Suggested Charter for an International Trade Organization of the United Nations. See U.S. Dept. of State Pub. No. 2598, Commercial Policy Series No. 93 (1946), P. III (hereinafter cited as *Suggested Charter*).
- 9 The Havana Charter also known as ITO Charter began with a Suggested Charter submitted by the U.S. delegates. It was intended to be a founding charter of the ITO. The GATT which was deemed only provisional would have been out of force, should the Charter had been approved and ITO established. Unfortunately, the Charter was aborted and the GATT consequently has been used to date. For detailed description of ITO Charter negotiations, see R.E. Hudec, *the GATT Legal System and World Trade Diplomacy* (1975 Praeger Publishers), pp. 14-17.

- 10 This approach is suggested by Prof. Bernier who concludes that, "if state trading is accepted as an alternative method of intervention of state in economic matters, its treatment should remain basically consistent with that granted by the GATT to other methods of intervention." GATT has overwhelmingly adopted a "material injury philosophy" in dealing with the injurious effects resulting from dumping and subsidization. Bernier, "State trading and the GATT", in *STATE TRADING IN INTERNATIONAL MARKETS* (1982 Kostecki ed.), pp. 257-58.

P A R T T W O

OVERVIEW OF THE GATT FRAMEWORK AND NON-MARKET ECONOMY

2.1 HISTORICAL BACKGROUND

The failure of the peace and economic cooperation efforts made by the League of Nations and Woodrow Wilson's Fourteen Points indirectly led to the Great Depression and World War II.¹ The lessons and experience of these incidents were reflected in the post-war multilateral system.² It became increasingly clear after the War that prosperity can be achieved through economic co-operation and global or regional trade liberalization.³

Post-war multilateral framework was based on numerous international and regional organizations which were designed to redefine the common interests of the international society and normalize international relations. The General Agreement on Tariffs and Trade (GATT), International Monetary Fund (IMF) and World Bank Group (formerly known as International Bank for Reconstruction and Development - IBRD) were formed to reduce national economic barriers and increase world economic prosperity.⁴ In addition, some regional organizations such as European Economic Community (EEC),⁵ Organization for Economic

Coordination and Development (OECD)⁶ emerged to promote regional economic management. They have been endeavoring to achieve world economic unity through regional cooperation.

Following the formation of the UN to secure world peace and unity, the international community became committed to construct a new international economic order that would dismantle trade and monetary barriers which were the main cause of the Great Depression and World War II.⁷ Several world-wide conferences, such as the Bretton Woods Conference (1944),⁸ and conferences held at London (1946), Geneva (1947) and Havana (1947-48), attempted to establish the IMF and International Trade Organization (ITO) both of which were aimed to provide a set of common rules and code of conduct to be observed in international economic relations.⁹

The GATT has now been in force for three decades as the central legal regime of international trade. It is a multilateral international treaty which first came into effect on January 1, 1948, and has now been acceded to by more than 86 nations. Most trading nations are GATT members with the exception of some of the Comecon (CMEA) countries, China, Mexico and some OPEC countries.

The drafting of GATT was largely associated with the U.S. trade policy.¹⁰ The spirit behind the General Agreement can not be properly understood without reference to the views of the American delegates because post-war international economic order was largely influenced by American policy.¹¹ The goal the U.S. negotiators sought to achieve was to establish an

economic order promoting free and non-discriminatory trade under which non-tariff barriers would be removed and tariffs reduced through international negotiations.¹² With these goals in mind, the American negotiators at the London Conference suggested a model charter to be used as a founding charter of the ITO.¹³ In the mean time, tariff negotiation was being conducted at Geneva Conference. Unfortunately, however, at the time of ITO Charter negotiations, the major trading states were not ready to commit their trade policies to such an international organization, and the ITO Charter (also known as the Havana Charter since the negotiations were held at Havana) failed to receive the ratification necessary to bring it into operation.¹⁴ The failure of the ITO Charter was rooted in the many exceptions and escape clauses in its provisions.¹⁵ Moreover, because the ITO Charter was designed to incorporate the Soviet state trading economy into its provisions, the non-participation of the Soviet Union in the Charter negotiations made much of what the American had suggested meaningless.¹⁶

However, a Protocol of Provisional Application was successfully signed by 23 nations at the Geneva Conference. The protocol provisionally brought the GATT into force pending a later adoption of the ITO Charter.¹⁷ Due to the abortion of the ITO Charter, the ITO never came into being and the GATT was forced to play the role of a major international trade organization with the objective of trade liberalization.¹⁸ Under the auspices of GATT there have been seven major rounds

of tariffs and trade negotiations including the on-going Uruguay Round.¹⁹

The successful reconstruction of the post-war international political and economic order is largely attributed to the painful lessons of the Great Depression and World War II.²⁰ The wave of the so-called "new multilateralism" in trade is the direct result of multilateral negotiations of major economic powers. But not all countries were active participants in this new wave of multilateralism. Some developing countries were then politically and economically dependent and unable to have a say in the formation of those trade rules. Many countries were not members of the GATT; for example, the Soviet Union, China, East Germany, Venezuela, Mexico and most Middle East OPEC countries. Thus GATT, as an international organization, was not representative of the whole world. Its role in international regulation has been limited to some major trading countries.

Admittedly the dream of achieving world prosperity and global peace through free trade has been partially fulfilled through GATT despite the fact that some important nations remain outside the GATT. However, the goal of global trade liberalization still has a long way to go.

2.2 COMPARATIVE ADVANTAGE AS THE PIVOT OF GATT

The GATT system rests on an underlying economic theory which holds that international trade serves to increase global

prosperity, as well as the prosperity of individual trading countries.²¹ It also rests on the concept that an orderly trade system governed by widely accepted rules for world trade lessens the risks of trade wars and thus is an essential part of broader efforts to maintain durable world peace and stability.²²

The fundamental belief of the GATT is "free trade" on the basis of the classic theory of comparative advantages.²³ Free trade, as opposed to protection, is a policy by which a government does not discriminate against imports in favor of domestic products or interfere with exports in order to favor consumers in the home market.²⁴ The benefits of free trade were advanced by the Scottish philosopher Adam Smith in his classic theory elaborated in *Inquiry Into the Nature and Causes of the Wealth of Nations* (1776).²⁵ Smith's theory was further elaborated by the English School of classical economists headed by David Ricardo (1772-1823), who propounded the theory of comparative advantage.²⁶ The argument for "free trade" on a comparative advantage was systematized by John Stuart Mill (1806-73)²⁷ and accepted by the majority of economists well into the 20th century.²⁸

However, free trade can hardly be absolute. Government intervention might always be justified on non-economic grounds.²⁹ Protectionism always exists due to conflicting interests of nations. In some situations, pure economic theory may conflict with the national interests of a particular country. Political and economic realities may pressure the

government into enacting protectionist restrictions on trade.³⁰ Also, individual nations always have domestic and foreign political goals that are motivated by policy concerns other than maximizing output.³¹

Obviously protectionism poses an economic problem to exporting countries. Initially, bilateral commercial treaties in which reciprocal tariff concessions and removal of trade barriers and other formalities were agreed upon, were seen as the way to reduce the impact of protectionism.³² Clauses such as "national treatment", "minimum international standard", and "most favored nation"(MFN) were adopted to afford legal security to international enterprise and investment under progressive international law.³³

With the inception of the new multilateralism under the GATT, the principle of non-discrimination in terms of MFN clause and national Treatment was incorporated as an essential ingredient of free trade.³⁴ The main goal of the GATT is to create a free-trade world market on the basis of nondiscrimination,³⁵ to provide a set of common rules within which individual trading countries conduct their trade with one another, and to provide an international forum for periodic or emergency negotiations of international trade and tariffs. Based on the notion of non-discrimination and trade liberalization, all tariff barriers are to be reduced to the lowest possible level. The results of tariff negotiations "on a reciprocal and mutually advantageous basis" are binding and unwithdrawable unilaterally.³⁶ The general objective was the

reduction of tariff barriers. Modification of the established Tariff Schedule could only be done through the process of "renegotiation", "consultation" and "conciliation".³⁷ Otherwise other contracting parties affected are entitled to withdraw or modify substantially equivalent concessions as a retaliatory measure.³⁸

All non-tariff barriers (NTBs) which hinder free-trade are to be removed through multilateral negotiations or renegotiations.³⁹ Tariffs as opposed to other instruments or measures should be the main weapon for import controls or for the protection of domestic industry.⁴⁰

However, GATT tolerates certain level of protectionism, such as the use of antidumping and countervailing duties,⁴¹ state-trading,⁴² and other direct or indirect trade controls,⁴³ including, in special circumstances, notorious safeguard or "escape clause"⁴⁴ and a general waiver procedure.⁴⁵

Protectionism is particularly strong in times of world economic depression or when a country experiences economic problems such as slow economic growth, shrinking domestic markets, high unemployment, and severe debt problems.⁴⁶ New forms of protection emerged together with the GATT permitted protectionist measures.⁴⁷ A disturbing feature of the more recent trade controls is the trend towards imposing protectionist measures under bilateral or unilateral arrangements outside the GATT framework.⁴⁸

As noted earlier, the GATT multilateralism is a compromise of trade protectionism and trade liberalism. This compromise somewhat balances the conflicting interests between producers, on the one hand, and consumers, on the other.⁴⁹ As the GATT system is framed basically in favor of free trade, its rules are largely concerned with the producers and traders of goods, and with the laws and policies of governments in support of these enterprises.⁵⁰ GATT rules are little concerned with broader aspects of domestic economic policy or with the interests of consumers. Nonetheless, GATT does obligate its members not to institute domestic trade policies that negate free trade.⁵¹

In summary, the post-war GATT multilateralism is a compromise between trade liberalism and protectionism. The ultimate objective of GATT remains the institution of an international economic order that promotes free and fair trade. However, the forces of protectionism remain strong in the present world and subtle and smart measures are being used to sidetrack GATT rules. The challenge for GATT is to ensure that these protectionist forces do not wipe away the progress made so far in promoting free and fair trade.

2.3 NME AND GATT MULTILATERALISM

2.3(1) CONFLICTING IDEOLOGIES: RECONCILABLE?

The end of World War II divided the developed world and some of the developing world into two parts: the East and the West. The two parts are based entirely on different systems and ideologies. One is based on the socialist system and communist ideology; and the other is on the market system and capitalist ideology. These two ideologies remain in constant conflict. At the economic level, the cause of conflict is obvious. While the "capitalism"⁵² is founded on the principle of minimal government intervention in the private enterprise economy, "socialism"⁵³, by contrast, revolves around wholesale government regulation of the economy. The government in NME not only owns the economy, but controls the daily life of its economic entities.⁵⁴

Under capitalism decision concerning production are made by private enterprises operating for private profits and laborers are free to work for the owners of the means of production.⁵⁵ In sharp contrast to capitalism, communism is a system of social organization which is based on common property, or an equal distribution of income and wealth.⁵⁶ Market economy is the expression of capitalism in economic terms. Under the market economy, the doctrine of free competition requires that there be very little government

intervention in the economy.⁵⁷ By contrast, socialist countries adopt central planning as a basic form of their economies.⁵⁸

Most Western countries including Japan follow the pattern of market economy, whereas the Soviet Union, China, Eastern European countries all adopt Marxist economic theory.⁵⁹ For NMEs their political systems are concentrated on the power politics of central committee of the Communist Party. There is virtually no separation between party politics and government management. Party politics dominates almost every aspect of their economies. The thrust of their economies, as will be seen later, is directed and manipulated by government officials along party lines.⁶⁰ The economy is not regulated by market forces of supply and demand, but rather is controlled at the center by the government.⁶¹ Because these economies are centrally planned and supposedly manipulated, they are often inflexible and distorted. The distortion arises from the fact that government intervention prevents the efficient allocation of resources.⁶²

Despite the conflicting ideologies and differences in political and economic systems, post-war international relations between East and West have been reshaped. As years go by, tension between East and West has been eased in the sense that "cold war" has been replaced with *detente*, economic embargoes reduced and *rapprochement* established. The volume of East-West trade has also increased. What is more noteworthy is the fact that when the capitalist world suffered from cyclical

economic fluctuations, strengthened government intervention, state-trading and other measures of protectionism,⁶³ the socialist system in the Eastern European countries, USSR and China, had revealed critical problems that needed radical economic and political reform.⁶⁴ Consequently, the two economic systems seemed to be drawing closer together by changes converging from both directions.⁶⁵ It is this changing situation that leads us to perceive the possible reconciliation of East-West trading systems.

2.3(2) GATT FRAMEWORK: A LEGAL AND STRUCTURAL OVERVIEW

If the Havana Charter reluctantly purported to tolerate the Soviet state trading systems so as to integrate them into a single international body-the ITO, GATT, as a traders' club, was to exclude from its membership centrally planned economies, normally referred to as NMEs. This is because the GATT's fundamental belief is based solely on market conception and ideologies which are incompatible with socialist NMEs.⁶⁶

From the historical and textual perspective, GATT is mainly aimed at dismantling tariff barriers, increasing transparency of signatories' trade regulations and policies, and providing a forum for international coordination and negotiation.⁶⁷ GATT comprises four parts. Part I lays down foundations for national trade legislation and trade policy. It consists of two Articles which demonstrate the purpose and cardinal principle of the General Agreement and consolidate

the established tariff Schedule.⁶⁸ Admittedly, non-discrimination constitutes the core of the GATT multilateralism. It is generally believed in the West that liberalizing trade barriers and eliminating discriminatory measures foster world economic prosperity and that the application of non-discriminatory principle assures security of market access and thus underwrites investment to exploit comparative advantage and specialization.⁶⁹ Beyond that, minimal government intervention is also considered vital to the promotion of competition and economic well being.⁷⁰ GATT is designed to fulfill this objective. Its rules are formulated to ensure minimal government intervention in international trade.

The foundation of modern international trade rules among industrialized countries is non-discrimination.⁷¹ The famous MFN clause (Article) is an overall demonstration of this principle, which requires that:

"any advantage, favor, 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 territory of all other contracting parties."⁷²

This is comprehensive enough to cover not only customs duties and charges, but also all rules and formalities concerning imports and exports. This is further strengthened by a requirement that any modification of concessions agreed on among certain GATT countries be accorded to all other GATT members automatically, unconditionally and multilaterally.⁷³

In theory, many of discriminatory bilateral trade agreements entered into between NMEs, such as Eastern European countries including China and GATT countries are incompatible with the GATT principle. Those agreements are characterized by the import commitments or quota allocations, and preferential tariff treatment.⁷⁴ All of them have certain component of counter-multilateralism and discrimination.⁷⁵ But in practice, within GATT, non-discrimination is not absolute. Article 1, while providing for the MFN obligation also provides for grandfather rights for existing margins of preferences but specifies that the margin may not be increased.⁷⁶ The MFN obligation is further qualified by the entitlement under Article 24 under which two or more countries may enter into customs unions and free trade areas to eliminate trade barriers between them and withhold such treatment from other contracting parties to the GATT.⁷⁷ The rationale for this major exception is that such arrangements are trade-creating, and will convey compensating benefits to non-participants.⁷⁸

In addition to those exceptions, reciprocity often prevails over non-discrimination. This was particularly true during the negotiations on some of the East European countries' accession to GATT. As a solution to market access to Poland and Romania, an import commitments approach rather than non-discrimination was adopted.⁷⁹

Part II provides basic commercial policies and code of conduct to be observed in international trade matters by participating countries.⁸⁰ It comprises 21 articles, providing

rules of national treatment for foreign imported goods and goods that are domestically manufactured or processed.⁸¹ Articles 7 and 9 clarify the rule of origin for the purpose of customs evaluation. Article 6 authorizes the imposition of antidumping and countervailing duty to remedy the injurious effects resulting from unfair trade practices such as export subsidies and dumping. While Article 11 requires the implementation of tariffs as the main instrument of trade policy in protecting domestic industries and regulating import and export trade, Article 18 prohibits export subsidies but exempts governmental assistance to economic development in the case of developing countries. Furthermore, Article 19 specifies the circumstances in which the government can invoke emergency safeguard measures. In addition to these substantive rules, Part II also contains some procedural rules for dispute resolution, such as "consultation" and "conciliation" in Article 22⁸² and "nullification and impairment" in Article 23. These procedures are re-emphasized in Part III of the GATT.

Part III contains rules which are mainly concerned with procedural problems. However, some of the rules can be considered as dealing with substantive problems. For example, Article 24 deals with customs union and free trade areas and Article 35 deal with non-application of the Agreement between contracting parties. The procedural rules also deal with joint action of the contracting parties under Article 25 and accession under Article 33.⁸³ Moreover, a three year periodic

and "special circumstance" re-negotiations process is provided for withdrawals and modifications of the Tariff Schedule.⁸⁴

Sometimes, the application of the procedural rules leads to the suspension, modification or withdrawal of obligations under the GATT.⁸⁵ However, any invocation of suspending or withdrawing procedures is only possible under certain conditions, and must have the approval of the Contracting Parties.⁸⁶ Such approval may be before or after the invocation.⁸⁷ Moreover, countries invoking exceptions and various safeguard procedures must also seek consultation with all the parties concerned and with the organization.⁸⁸ In most cases compensation must be negotiated, otherwise the affected contracting party may retaliate.⁸⁹ This indicates that GATT law should be viewed not only as a set of substantive rules but also as an elaborate set of procedures. The aim of these procedures is not only to make GATT rules amenable to changing circumstances, but also to provide a dispute settlement mechanism. It also serves the common economic and political interests of members in the complex and ever-changing economic and political situations. The procedures also help to form public opinion within the organization thus allowing for collective persuasion and pressure.⁹⁰

Part IV entitled "Trade And Development" was added to GATT rules in 1965 to address the importance of exports in increasing the living standards of Less-Developed-Countries (LDCs).⁹¹ Part IV constitutes one of the major changes or exceptions to the original GATT framework. It provides special

rules and treatment for trade with developing contracting parties including LDCs.⁹² It is the origin of Generalized system of Preferences (GSP)⁹³ and the third world trading club - the UN Conference on Trade and Development (commonly called UNCTAD).⁹⁴

While the MFN clause is aimed at dismantling discrimination against foreign goods at the border, the national treatment clause is designed to prevent discrimination against imported goods in a contracting party's internal market. Non-discrimination enunciated in the twin clauses of the MFN and national treatment is foremost policy of the GATT. As Gerard Curzon said:

"Non-discrimination is probably the most important single concept that informs GATT. Bilateralism, quantitative controls, extension of preferences, state trading and all similar tools of commercial policy are in principle anathema to the Contracting Parties because they make inevitable the preferential treatment of one country as against another for other than commercial reasons."⁹⁵

Non-discrimination is a means to achieve trade liberalization. The concept of trade liberalization is partly realized by tariff reductions effected on a reciprocal, non-discriminatory basis. The result of negotiations on a reciprocal and mutually advantageous basis shall be bound and unalterable unilaterally.⁹⁶ Only through renegotiation or consultation can the established schedule be withdrawn or modified.⁹⁷ Moreover, the level of modified schedule should not be in excess of previous agreed schedule.⁹⁸ It is thought that with continuous tariffs concession, tariff barriers restricting trade will be eventually removed.

Due to the difficulties in realizing global integration, the goal of trade liberalization is expected to be first accomplished by regional integration. This is often justified on the ground that countries with similar level of economy, relatively similar culture, base norms and traditions are easier to integrate. Examples are the Benelux customs union, European Economic Community, Canada-U.S. Free Trade Agreement and so on. In many provisions GATT expressed its aspirations in achieving integration of world trade.

However, in finding reciprocity formula GATT countries are extremely pragmatic and materialistic. This is particularly true when contracting parties try to formulate tariff concessions with almost mathematic precision.⁹⁹ Almost every substantive rule has been softened by its flexible exceptions. This shows the tension between the poles of "legalism"¹⁰⁰ and "pragmatism."¹⁰¹ The two equally strong poles decides the legal nature of GATT to be a combination of "norms of obligations" and "norms of aspirations".¹⁰² Admittedly, GATT has a lofty goal in mind, but it is unattainable as long as protectionism remains strong. Exceptions and escape clauses have to be attached and delicately elaborated to prevent the collapse of the GATT regime. It is a sort of "soft law" as opposed to "hard law".¹⁰³ The softness of the GATT law is implicit in its softly and vaguely formulated rules. It is this softness that encourages a flexible almost discretionary interpretation.

However, one must note that it is not the vagueness of their formulation that makes the GATT rules "soft", but rather the numerous exceptions and various procedures that may be invoked soften obligations that are too rigid to suspend or withdraw. GATT was intended to contain precisely formulated rules especially when negotiating tariff concessions. The flexibility coupled with vagueness reflects the intricacies of negotiations. It also reflects a compromise of conflicting interests representing trade liberalism and protectionism.

A careful overview of the GATT legal framework enable us to summarize GATT principles as follows¹⁰⁴: (1) Nondiscrimination (MFN clause and national treatment); (2) reciprocity; (3) consolidation; (4) generalization and liberalization; (5) tariff negotiations on a product-by-product basis;¹⁰⁵ (6) consultation and conciliation; (7) transparency;¹⁰⁶ (8) tariffs protection. Attached to those principles are following essential exceptions, namely: (1) GSP system;¹⁰⁷ (2) linear or plan target negotiations (to find asymmetric reciprocal formula for NME's accession); (3) retaliation (if compensation is not offered or cannot be negotiated); (4) remedies for unfair trade practices by taking advantage of free trade (including invoking safeguard-escape clause, imposing antidumping and countervailing duty, and other admissible forms of remedies. Note that they should generally be used on a temporary or emergency basis); (5) regional integration (Article 24).

A fundamental tenet of GATT is that tariffs are the only admissible form of protection. This policy is based on the conviction that tariffs as compared to other trade instruments such as subsidies, state trading, permit price competition, has the least interference with allocation of resources. They are more visible, less flexible and more capable of being negotiated downwards and administered on a non-discriminatory basis.¹⁰⁸

It is true, however, if one contends that GATT is a typical compromise between trade liberalism ("mainstream") and protectionism ("branch stream"). It is also true if one argues that the GATT rules are "weakly enforced, easily avoided, and widely abused".¹⁰⁹ Yet, the overwhelming theme of the GATT law is nondiscrimination and trade liberalization. Thus one should not attach too much weight to the exceptions and flexibility. Also, the function of the GATT regime should not be underestimated just because of its "softness". The GATT not only creates a sponsorship or a forum for international negotiations, it also plays a decisive role in regulating, compromising, and supervising diverging national commercial and trade policies of each individual participant.¹¹⁰ In a sense GATT should be viewed dynamically rather than statically. It should be viewed as a continuing process of international negotiations on trade and tariffs. As prescribed in GATT, results of negotiations should become an integral part of the General Agreement.¹¹¹ Moreover, many of the GATT

rules benefit trading countries-especially those who have the same or similar level of economic development.

Having addressed this, it should be added that the GATT regime has many shortcomings and even a degree of unfairness if one looks at it from the perspective of developing contracting parties, or NMEs whose economies are either underdeveloped or substantially different from Western developed economies. Some GATT rules, such as rules against dumping and subsidies are simply inapplicable to NMEs.¹¹² Others including rules on state-trading, quantitative restrictions on imports are hardly enforceable in the context of centrally planned, target-protected NMEs.¹¹³ Thus global trade integration remains a dream, and the unfavorable GATT environment to NMEs is yet to be improved.¹¹⁴ The reason for these drawbacks can be found in its very fundamental assumption. As the GATT law is almost exclusively formulated in favor of free trade on a private enterprise basis along the pattern of market economy, there is virtually no place for nonmarket economy countries to have an effective access. As one professor well put it:

"many of the GATT rules make sense only in the context of such a market system, since they restrict the types of regulations which governments can impose on international traders, but do not purport to regulate the traders themselves."¹¹⁵

This limits the extent to which GATT rules can be applied. This makes the problem of integrating NMEs into the GATT very difficult. It is also said that GATT rules,

especially rules on state trading fit poorly into the NME because:

"the [GATT] system presupposes that importation and exportation are handled by private firms which, stimulated by profit motives, are guided by commercial considerations."¹¹⁶

2.4 NME'S GATT MEMBERSHIP: ISSUE OF COMPATIBILITY RAISED

2.4(1) EVOLUTION OF EAST-WEST RELATIONSHIP

Following the abortion of the Havana Charter upon which the ITO was supposed to be based, GATT became a "richmen's club" or a traders' club mainly beneficial to Western market economies.¹¹⁷ The socialist Eastern bloc turned away from the GATT largely due to the irreconcilability of their political ideologies and economic systems with the GATT preferred market ideology and minimal government intervention in economy. Another reason was due partly to their misunderstandings of the prospect of capitalist world.¹¹⁸ Despite the tension resulting from different systems, the Eastern bloc's attitude and belief have undergone fundamental changes since late 1950s.

An overview of the East European countries' attitude towards the GATT would show that they have gone through at least three distinct stages: from the initial entire rejection (1947-55) to the partial acceptance (1955-66) and to the full acceptance (1966-70s).¹¹⁹

The initial stage of rejection was based on the following historical reasons and political considerations: In the late 1940s the Soviets believed that the real objective of the American plan for the post-war economic order was to build U.S. domination over world politics and economies.¹²⁰ They firmly believed that so-called non-discriminatory and multilateral trade, freer trade, better investment opportunities along with economic aid were nothing but strategies to increase this domination.¹²¹

Moreover, multilateral and free trade principles were in direct conflict with the Soviet state-trading system and centralism. There seemed no room for compromise.¹²² Also, the Soviet Union cautiously noticed that East European accession to GATT would carry a risk leading the U.S. to expand its economic and political power into the Soviet sphere of influence.¹²³ Furthermore, the Soviet as well as East European countries expected that the capitalist might suffer another greater economic crisis and, as a result, capitalist system would evolve to be more centralized.¹²⁴ This premature prediction together with Soviet political considerations and distinct economic and trade system had kept them away from participating in the GATT. As an alternative, they prefer bilateral trade as a more advantageous deal.¹²⁵ Finally, there existed at that time certain contradictions between the Western concept of non-discrimination, multilateralism and the method of country-specific planning in foreign trade sector of both Soviet Union and Eastern Europe.¹²⁶ Compliance with non-

discrimination could require substantial reforms in their planning methods.¹²⁷

The later change in the East European attitude grew from a complex political and economic developments. The experiment of the market-type GATT trading system consequently made them to realize that the GATT-based trade order promoting freer trade, non-discrimination and multilateralism would be in the interests of small- and middle-sized traders. Another important reason was that the strong vitality of capitalism disproved the Marxist prediction that the capitalist world would suffer another economic crisis greater than the depression between 1929-33. Such change of attitude towards market-type of GATT was theoretically justified by the then wide-spread doctrine of "peaceful co-existence"¹²⁸ which holds that since socialism prevails only in some countries, one must imply a necessary period of coexistence between countries with a socialist economy and those with a capitalist economy. The peaceful coexistence of two different systems was the only option left if the peace were to be maintained.

2.4(2) NME MEMBERSHIP IN GATT

Based on the above-indicated considerations, mutual understandings and changed environment in the sphere of East-West relationship, many of the East bloc countries began expressing their genuine and strong interest in participating in the GATT system.¹²⁹

Poland was the first to indicate its interest in joining the GATT in 1957.¹³⁰ Following that Romania showed its desire to be admitted into GATT club in the same year.¹³¹ However, these two countries joined the GATT on the basis of import commitments as a reciprocity formula solving the market access issue.¹³²

Following the Polish and Romanian interest in joining GATT, Hungary launched its request for observer status in the GATT in 1958.¹³³ Although the initial application was frustrated, from the mid-1960s on, Hungary was preoccupied with the reform aimed at increasing the market role in the domestic economy and foreign trade.¹³⁴ The reform made possible partial adjustment of the Hungarian trade regime to the traditional GATT system. When Hungary presented its second request for observer status in 1966, it was accepted without complications. Noticing the weakness of the Polish and Romanian pattern, and having enough lessons from their negotiations with GATT, Hungary doggedly believed that to have an effective access to GATT and GATT markets, a country's economy and trade conduct should be compatible with the GATT requirements. Based on this belief it bravely adopted a "new economic mechanism" commencing 1968 and remarkably decentralized its economy.¹³⁵ The reform enabled her to accede to the GATT on the basis of tariff negotiations in 1973.¹³⁶

When Yugoslavia was accepted by the GATT, its economy had already been treated as if it were a market economy.¹³⁷ From the moment of its break with the East European bloc(1948),

Yugoslavia progressively engaged in the decentralization process to establish a so-called "market socialism".¹³⁸ The removal of political obstacles kept her closer to GATT.¹³⁹ Further reforms resulted in the introduction of tariffs, abolition of multiple exchange rates, simplification of trade control, and thus brought the Yugoslav economic and foreign trade system far closer to the requirements of GATT.¹⁴⁰ At the time of its full accession in 1966, Yugoslavia claimed to use tariffs as the only instrument of trade control under normal conditions. The State trading mechanism was said to be used only on an occasional basis.¹⁴¹ There existed free price formation, a unified exchange rate and no export subsidies. And it administered its desirable QRs in a nondiscriminatory fashion.¹⁴²

Czechoslovakia had original membership in GATT and so had no accession problem when its economy became nonmarket type of state trading in 1948. Nonetheless, the U.S. reserved its right to apply MFN treatment to Czech and some other GATT members retained QRs on Czech imports.¹⁴³ The same situation was faced when Cuba became a satellite of the Communist bloc.¹⁴⁴ Bulgaria has been an observer in the GATT since 1967 and was active in the Tokyo Round negotiations. But it never became a member.¹⁴⁵

Beyond East European bloc, China has expressed its interest in participating in GATT.¹⁴⁶ The interest became clearer when China signed the Multifibre Agreement and

acquired observer status in many of the GATT-sponsored international negotiations.¹⁴⁷

Interestingly enough, even the USSR attempted to acquire an observer status in the Uruguay Round negotiation with an interest in seeking its full GATT membership in future.¹⁴⁸ Not surprisingly, its request has been rejected by the majority of GATT countries.¹⁴⁹ Perhaps the Soviet application is worth reconsideration since the Soviet union seems the last stronghold of the socialist bloc.

The above survey enables us to conclude that the diversity of East Europe's foreign trade systems explains why different models have been applied to each country. Among the five socialist countries admitted to GATT, Poland, Romania and Hungary are most revealing cases in the context of NME's accession to GATT. Czechoslovakia entrance provides little experience for reconsidering the technicalities of East-West trade relationship. Yugoslavia, though once a centrally planned economy, entered the GATT claiming tariff protection, internal competition and the absence of state trading. It is Poland's *rapprochement* with GATT that provides the first opportunity to negotiate some concrete technical arrangements for target-protected (as opposed to tariff-protected) economies in GATT. The Polish model was most closely followed by Romania and somehow influenced Hungarian negotiations with GATT. Hungarian formula of accession was made possible by the broad decentralization of its economy. Together with Yugoslavia, Hungary's approach provides NME's new-comers to

GATT with very useful precursory experiences of reconciliation.

2.4(3) ISSUE OF COMPATIBILITY RAISED-GENERAL FINDINGS

When Eastern European countries were applying for GATT membership, the most frustrating problem was the compatibility of their state trading system with the GATT requirements, and applicability of GATT rules-such as subsidies and dumping to their NMEs. At that time many of theoretical and structural problems within the GATT legal framework had been neglected. Both GATT CPs and East European countries were overly concerned with reciprocal exchange of benefits and rights. They blinked at the cardinal principle of nondiscrimination. Instead of solving theoretical and structural incompatibility of NMEs with GATT, most of GATT CPs especially Western European CPs were more interested in finding a fast and pragmatic solution.¹⁵⁰ They were more concentrated on finding a reciprocity formula to solve the most crucial issue of market openings in both directions.¹⁵¹ As a result of their pragmatism along with the Eastern Bloc's haste in obtaining admissions, the approach invented was import commitments-a very pragmatic way of admission and yet at surprisingly cheap cost.¹⁵² The approach has suffered fatal weakness which will be seen later, and it is virtually inapplicable to the case of China's accession problem.¹⁵³ It has been ineffective in fostering the growth of East-West trade. As to Eastern Europe,

it won the battle of obtaining the certificate of GATT membership but lost the war against Western CPs' discrimination. This results from their neglect of such essential presumption on which GATT has long been founded. Such assumption requires in the first place that GATT members' economy be tariff-protected and essentially private enterprise economy with minimal government intervention. Free trade with non-discrimination and fair trade with minimal government intervention is the substance of GATT.

The main purpose of the thesis at this time is therefore to discuss more theoretical and structural problems which have been ignored both in academic and official circles. To this end it is unavoidable to analyze whether the GATT major rules are compatible with NME and whether the GATT can be used as an adequate and effective framework in integrating the NME into world trade. In examining the compatibility of GATT framework with NME, a brief comparison of characteristics of NME and function of free-market economy (FME) is necessary to deepen our understanding of the subject.

FME v. NME: In a FME, international trade is conducted by the independent decisions of buyers and sellers acting out of economic self interest.¹⁵⁴ Prices set by the market are used to allocate scarce resources.¹⁵⁵

But in NME, key investment, production, purchase and distribution decisions are, for the most part, determined not by market forces, law of supply and demand, but by state planning.¹⁵⁶ Their international trade and resources

allocation are also regulated by state planning with little commercial considerations of cost-benefit.¹⁵⁷ Their prices do not have the same meaning as in FME because:

"Not only are the prices of NME enterprise controlled, but its costs...also are centrally determined. With administered costs and prices, profits are effectively administered as well. Finally, economic activity is centrally directed through the use of administrative prices, plans and targets."¹⁵⁸

In FME the price of a product tends to influence both the quantities for consumption and production, whereas in NME the prices have little influence on production quantities.¹⁵⁹ In NME production quantities are planned in advance and the price for a particular product is set at a level that will clear the market.¹⁶⁰

Furthermore, tariff rates in NME have a much more limited influence on the level of imports than that in FME.¹⁶¹ The tariff schedule in NME is not essential in determining the origins of imports, and a MFN commitment can be discharged simply by imposing identical tariffs on imports from all countries. The reason for this lies in the fact that most importing agencies in NME follow political criteria rather than so-called "commercial considerations" in selecting foreign suppliers and uniformity of customs duties is irrelevant.¹⁶² Even if the determination of the sources of imports follow commercial considerations, the NME's planning authorities can still use internal pricing power to influence the choice of those sources, particularly when imported goods are functionally similar but physically distinguishable.¹⁶³

The incompatibility of NME system with market economy is worsened by the inconvertibility of its currencies and duality of its exchange rates.¹⁶⁴

Finally, the NME system can exclude foreign products from its market through administrative control over purchasing or pricing decisions, without recourse to tariffs or the non-tariff measures traditionally subject to GATT regulation.¹⁶⁵ Such system creates a dilemma for the market-oriented GATT and so it is difficult to integrate NME into the GATT trading system. It also makes reciprocity between the East and West trade elusive and undercuts the general principle of non-discrimination.

Despite the above indicated differences, FME and NME share certain similarities particular to the case of their political influence on state trading enterprises (STEs). STEs of both economies may favor one foreign source over another on the non-commercial grounds.¹⁶⁶ For instance, U.S. because of its over-whelming ideologies embargoed all the imports for communist countries during the cold war.

Also, it is worthwhile to notice some institutional changes in both NME and FME systems that have blurred the distinction between NME and FME.¹⁶⁷ For instance, in order to reduce informational inaccuracy or inefficiency and the number of decisions to be made by the central planners, NMEs have been decentralized to some degree by introducing incentive systems¹⁶⁸ and price reform and by increasing the autonomous power of foreign trade organizations or corporations.¹⁶⁹ As a

result, some NME countries like Hungary, Yugoslavia, and China after their economic reforms turn out to be loose state trading countries.¹⁷⁰ Even in Poland, Romania and the USSR some measures of reform have been introduced. Is not Mr. Gorbachev propounding remarkable new thinking in reforming the Soviet economic and political structure.¹⁷¹ In FMEs on the other hand, government interventions including state trading activities have increased since the world war II. Many STEs as opposed to traditional private enterprises have been established in most of Western World.¹⁷² For example, Airbus in Europe,¹⁷³ the Wheat Board and beverage state trading in Canada,¹⁷⁴ unique administrative guidance measures in Japan,¹⁷⁵ and oil and some key products monopolies in the U.S., the U.K. and in almost every market economy.¹⁷⁶

Perhaps the difference between state trading in NME and FME is only a matter of degree. One is systematized and centralized whereas the other is using state trading only occasionally. Therefore there is nothing absolutely excluding NME countries from participating in the GATT-based world trade.

Nevertheless this does not diminish the earlier finding on the issue of compatibility of NME with the GATT. It can be concluded that unless NMEs opt to decentralize their centrally controlled, target-protected economic system and remove rigid, bureaucratic political obstacles to free trade, the effectiveness of their participating and competing in the

free-trade world under the promotion of the GATT is undoubtedly questionable.

In the past many scholars and practitioners talked about incorporating new rules into the GATT framework accommodating NMEs in GATT membership. This is not practicable since it will conflict with the well founded GATT regime and may cause it to collapse. This proposal has proven contradicatory in China and other similar NME countries. For example, Mr. Deng Xiaoping, one of the most senior leaders in China, wants capitalist market mechanisms to co-exist with central planning under his pragmatic thinking that "a cat is a good cat if it catches rats regardless of its being white or black". In the meantime he follows the communist ideology in its political structuring. Regrettably, this philosophy has caused problems in the course of economic reform. It is, in effect, not workable for the obvious reason that communist political ideology is simply incompatible with capitalist economic ideology.

While deciphering such incompatibility one should also consider the possibility of reconciliation in a way that much of the institutional changes in NME would ease the tension between the East-West relationship. As economic and foreign trade reforms continue to decentralize the economy, to loosen import controls measures, and to remove unnecessary trade barriers, the possibility of the two becoming reconciled will become bigger. As a matter of fact, some NMEs like Hungary, Yugoslavia are already compatible with the GATT fundamental

requirements. Other NMEs like Poland, Romania and China are also making efforts to integrate their economic system into the GATT system. Even the USSR and East Germany have started progressive economic reforms that will bring them closer to the GATT-required system. Nonetheless, most of those NMEs would have a long way to go before they can fill the gap with the western political and economic model.

At the present stage all that can be said is that NME and the GATT trading system will remain irreconcilable if neither the GATT system nor their state trading system is to be changed. However, they will be reconcilable if either the assumptions upon which GATT rules are based or upon which state trading systems of NMEs are based are to be changed.

Footnotes

- 1 Jackson, *Implementing the Tokyo Round* (1984), p. 11.
- 2 *Id.*
- 3 *Encyclopedia Britannica*: "Free Trade" (1978), Vol. 9, pp. 849-52.
- 4 Jackson and Davey, *Legal Problems of International Relations* (1986 2d ed.), pp. 281-84.
- 5 *Id.* pp. 199-204.
- 6 OECD was established in 1961 as an expanded successor to the Organization of European Economic Cooperation (OEEC). For a detailed explanation see M. Camps, *"First World" Relationships: The Role of the OECD* (Council on Foreign Relations, 1975).

- 7 Jackson, *supra* note 1, p. 11. (The basic themes to be considered in the post-war reconstruction center on: (1) the relationship of economic forces to the causes of war and the need to develop institutions that could preserve the peace; and (2) the economic theory of comparative advantage that supported a policy of trade liberalization). *Id.*
- 8 Gerald M. Meier, "The Bretton Woods Agreements--25 Years after" (1971) 39 *Stanford L.Rev.* 235, 237, 245-46. (The term "Bretton Woods System" incorporates the GATT as well as the IMF and World Bank, because the Bretton Woods Conference looked forward to the creation of an ancillary institution that would reduce obstacles of international trade and gives effect to the principle of multilateral nondiscriminatory trade).
- 9 E. McGovern, *International Trade Regulation--GATT, the United States and the European Community* (1982); K.W. Dam, *The GATT Law and International Economic Organization* (1970); J. Jackson, *World Trade and the Law of GATT* (1969); R. Hudec, *The GATT Legal System and World Trade Diplomacy* (1975)
- 10 For historic overview of the basic design of GATT, see R.E. Hudec, *The GATT Legal System and World Trade Diplomacy* (Praeger Publishers, 1975), pp. 44-46.
- 11 Dam, *supra* note 9, pp. 5-7.
- 12 *Id.* at 6.
- 13 London Report, UN Doc. EPCT/34 (1947); UN Doc. EPCT/c.6/w.55(1947).
- 14 With respect to the troubled history of the GATT, see J. Jackson and Davey, *supra* note 4, pp. 293-96; G. Curzon, *Multilateral Commercial Diplomacy* (1965); K. Dam, *supra* note 9, 10-16; R. Hudec, *supra* note 9, 4-53; K. Kock, *International Trade Policy in the GATT, 1947-67* (1969); P. Lortie, *Economic Integration and the Law of GATT* (1975); E. McGovern, *supra* note 9, p. ; G. & V. Curzon, "The Management of Trade Relations in the GATT" in A. Shonfield, G. & V. Curzon, T. Worley and G. Ray, *International Economic Relations of the Western World 1959-1971*, Vol. I: Politics and Trade (1976);. Diebold, *The End of the ITO* (Essays in International Finance No. 16, Princeton University Press, 1982).
- 15 Dam, *supra* note 9, pp. 13-14; see "The ITO Charter," *Fortune*, July 1949, p. 61. (An editorial subtitled "The ITO is all exceptions.")

- 16 Kostecki, *East-West Trade and the GATT System* (1979), pp.1-3.
- 17 Jackson, *supra* note 4, p. 295; Jackson, *supra* note 9, s.2.4.
- 18 Jackson, *supra* note 4, pp. 294-96. (Although it was not contemplated that the GATT would be an organization).
- 19 1947-Geneva negotiation of the original GATT, including the tariff schedules; 1949-And, France; 1950-Torquay, England; 1955-Geneva (tenth GATT session); 1960-61-the Dillon Round; 1962-67-the Kennedy Round; 1973-79-the Tokyo Round, or Multilateral Trade Negotiation (MTN); 1983-present-the Uruguay Round. For detailed discussion of the Tokyo Round, see Jackson, *supra* note 1.
- 20 *Encyclopedia Britannica*, *supra* note 3, pp. 845-49.
- 21 R. Blackhurst, N. Marian & J. Tumlrir, *Trade Liberalization, Protectionism and interdependence* (GATT Studies in Int'l Trade, No. 5, Geneva 1977).
- 22 Frank Stone, *Canada the GATT and the International Trade System: Essays in international economics* (1984), p. 14.
- 23 For discussion of law of comparative advantage, see C.P. Kindleberger, *International Economics*, 17-21, 27,33 (5th ed. 1973).
- 24 *Encyclopedia Britannica*, *supra* note 3, at 849.
- 25 Adam Smith, *Enquiry Into the Nature and causes of the Wealth of Nations* (1776), (hereinafter *Wealth of Nations*). (The central content of Adam Smith's argument was that division of labor leads to specialization, efficiency and greater production. Competition, in his eye, was of paramount importance to the growth of national economy and individual wealth. Government thus should as far as possible keep their hands off intervening in the affairs of private enterprises.)
- 26 David Ricardo, *Principle of Political Economy and Taxation* (1817). (explaining the advantages of specialization and contended that trade between countries was not dominated by relative costs of production, but rather by differences in internal price structures which reflected the comparative advantage of the trading countries and made exchange desirable.)

- 27 J.S. Mill, *Essays on Some unsettled Questions in Political Economy* (18) (giving solutions to the problems of the distribution of the gains of international commerce, the influence of consumption on production, the definition of productive and unproductive labour and the precise relations between profits and wages).
- 28 P. Samuelson, *Economics*, p. 692 (9th ed. 1973) (There is essentially only one argument for free trade or freer trade, but it is an exceedingly powerful one, namely: free trade promotes a mutually profitable division of labour greatly enhances the potential real national product of all nations and makes possible higher standard of living all over the globe).
- 29 J.M. Keynes, *General Theory of Employment, Interest, and Money* (1936) (using "full employment" as a criterion of economic policy to argue against free trade).
- 30 Stone, *supra* note 22, pp. 15-16.
- 31 Jackson and Davey, *supra* note 4, pp. 28-30.
- 32 *Encyclopedia Britannica*, *supra* note 3, pp. 850-52.
- 33 *Id.*; see also, Akehurst, *A Modern Introduction to International Law* (1987 6th ed.), pp. 87-103; David H Ott, *Public International Law in the Modern World* (1987, Pitman), pp. 176-89.
- 34 GATT Article 1: MFN clause coupled with "National treatment" (Article 3).
- 35 To quote preamble of the GATT, it is recognized that "economic endeavors should be conducted with a view to raising standards of living, ensuring full employment and a large and steadily growing volume of real income and effective demand, developing the full use of the resources of the world and expanding the production and exchange of goods...Being desirous of contributing to these objectives by entering into reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade and to the elimination of discriminatory treatment in international commerce.
- 36 GATT, Article 28 bis.
- 37 GATT Article 28 permits two kinds of renegotiation: three-year periodic renegotiation and "special circumstances" renegotiation (Article 28:4). The procedure as regards consultation with both cps concerned and CONTRACTING PARTIES and conciliation through the CONTRACTING PARTIES is valid throughout the dispute resolution.

- 38 GATT, Article 28:4(b).
- 39 GATT, Articles 28, 28 bis.
- 40 GATT Article 11 which provides that, "No prohibition or restrictions other than duties, taxes or other charges), whether made effective through quotas, import export licenses or other measures, shall be instituted or maintained by any contracting party on the importation of any product." Here other measures, according to an interpretive note, include "exchange control", "domestic price formation", "import mark-up" and state trading practices. This requirement is to dismantle the various means of government intervention or administrative control over imports. Or otherwise tariff negotiation will be meaningless if tariff is not main element of regulating trade.
- 41 GATT Article 6: so-called "Track I".
- 42 GATT Article 17 set forth commercial criteria on which state trading enterprises should observe.
- 43 GATT Art. 11 calling for general elimination of import licensing and quota system with several important exceptions. Although GATT tries to minimize the use of indirect trade controls such as "state trading", exchange control, voluntary export restraints, and other NTBs, their protective uses are prevalent.
- 44 GATT Article 19 provides that, in the case that, "any product is being imported...in such increased quantities and under such conditions as to cause or threaten serious injury to domestic producers...of like or directly competitive products", importing cp shall be free to suspend the obligation in whole or in part or to withdraw or modify the concession with respect to some imported goods.
- 45 GATT Art. 25:5- "in exceptional circumstances", the Contracting Parties may waive an obligation imposed on a CP by the GATT. This waiver is limited by 2/3 majority consenting vote of CPs. Interpretation of "exceptional circumstances" is within the reach of CPs. In practice, this is construed very broadly.
- 46 Stone, *supra* note 22, p. 3.
- 47 *Id.*
- 48 *Id.*

- 49 *Id.* (On the one hand, the GATT rules are designed to establish the rights of producers in one country to sell products in other member countries. On the other hand, the rules define and limit the freedom of governments to restrict the importation of goods and otherwise to protect their domestic producers against international competition).
- 50 *Id.*, p. 28.
- 51 *Id.*
- 52 Despite the existence of certain elements of inequality between workers and owners of the means of production, and despite the moral criticism, capitalism has long been considered as a better form of systems to increase social wealth. Capitalism, a victory over feudalism, reached its peak in western Europe with introduction of Adam Smith's great economic theory and influence of French "laissez faire" idea. Yet, capitalism met its valley when Russian Revolution uprooted over a vast area not only the basic institution of private property in the means of production, but the class structure, the traditional forms of government. *ENCYCLOPEDIA BRITANNICA*, Vol. 13, pp. 605-6.
- 53 For discussion of the Marxist-Leninist vision of socialism, see Gregory and Stuart, *Comparative Economic Systems* (1980), pp. 110-11; *Encyclopedia Britannica*, *supra* note 21, p. 851.
- 54 *Recent Economic Thought: Comparative Economic Systems: Present Views* (1984, Andrew Zimbalist ed.), pp.23-28.
- 55 Karl Marx (1818-1883), *Capital I*, 1867, pp. 638-650. {In Marx's original prediction Communism should overcome all the weakness of capitalism or should evolve from a highest stage of capitalism, which in Lenin's word is "imperialism", see Lenin, *Imperialism, the Highest State of Capitalism* (1916)}.
- 56 Marx, *id.*
- 57 Adam Smith, *Wealth of Nations*, 1776, pp. 74, 76, 100ff, 114ff.
- 58 Manuel Gottlieb, *A Theory of Economic Systems* (1984), pp. 209-215.
- 59 Gregory and Stuart, *supra* note 53, pp. 109-152, 284-318.
- 60 See *Comparative Economic System*, *supra* note 54, pp. 23-28.
- 61 *Id.*, 24-26.

- 62 *Id.*, 26-28.
- 63 Gregory and Stuart, *supra* note 53, pp. 168-187, 235-274.
- 64 *ENCYCLOPEDIA BRITANNICA*, *supra* note 3, p. 852.
- 65 *Id.*
- 66 Kostecki, *supra* note 16, p. 35.
- 67 Jackson, *supra* note 4, pp. 296-98 (outlining the basics of the GATT).
- 68 GATT Art.1: MFN Clause and Art.2: binding tariff Schedule.
- 69 *Id.*
- 70 Adam Smith, *Wealth of Nations*, 1776, pp. 111ff, 114ff; M. Gottlieb, *supra* note 59, pp. 83-89.
- 71 G. Schwarzenberger, "Equality and Discrimination in International Economic Law", 25 *Yearbook of World Affairs* 163, 163-65 (1971)
- 72 GATT Article 1.
- 73 GATT Article 2.
- 74 Kostecki, *supra* note 17, pp. 58-59.
- 75 *Id.*
- 76 GATT Article 1: MFN Treatment.
- 77 GATT Article 24: Regional Integration.
- 78 Para. 4 of Article 24 states that: "the purpose of a customs union or of a free-trade area should be to facilitate trade between the constituent territories and not to raise barriers to the trade of other contracting parties within such territories."
- 79 Kostecki, *supra* note 17, pp. 134-36.
- 80 The purpose of Part II is enunciated in Article 3 which aims at removing or reducing internal taxations and regulations which afford protection to domestic production. (para.1 of Article 3).
- 81 GATT Art.3: National treatment.
- 82 GATT Article 22 contains stage 1--bilateral consultation with cps affected and stage 2--Conciliation by the plenary organ- the Contracting Parties.

- 83 Article 33 makes a 2/3 majority sufficient for accession of a new nation to GATT; at the same time, Article 35, however, gives each existing party the privilege to refuse to apply GATT to the acceding country.
- 84 Article 27, 28, 28bis. For detailed analysis see Jan Kolasa, " Law-Making and Law Enforcing For International Trade: Some Reflections on The GATT Experience" in *World Order Studies Program Occasional Paper No.3* Center of International Studies (Princeton University, 1976), pp. 20-24.
- 85 Kolasa, *supra* note 84, p. 35.
- 86 *Id.*
- 87 *Id.*
- 88 *Id.*
- 89 GATT Article 27, 28.
- 90 Thiebaut Flory, *Le GATT Droit International et Commerce Mondial* (Paris 1969), p. 259.
- 91 GATT Article 36: Principles and objectives (paragraphs 1 through 8).
- 92 Para. 8 of GATT Article 36; see also Jackson, *supra* note 4, pp. 1138-61.
- 93 For discussion of GSP see Jackson, *supra* note 4, pp. 1154-61.
- 94 *Id.*, pp. 1141-53.
- 95 Gerard Curzon, *Multilateral Commercial Policy*, *supra* 14, p. 59.
- 96 GATT, Article 2(5).
- 97 Kolasa, *supra* note 84, pp. 19-28.
- 98 GATT Article 2(1)(c).
- 99 Kolasa, *supra* note 84, p. 31.

- 100 Dam, *supra* note 9. Where he refers "legalism" to an approach to the drafting of GATT under which draftsmen attempt to foresee all of the problems that may arise in a particular area and to write down highly detailed rules in order to eliminate to the greatest extent possible any disputes, or even any doubts, about the rights and obligations of each agreeing party under all future circumstances. *Id.*, pp. 3-4.
- 101 Dam, *supra* note 9. ("Pragmatism" is meant an approach to the drafting of the GATT under which emphasis is placed on mutual agreement on objectives, rules concerning rights and obligations are considered formalities to be avoided whenever possible.) *Id.*, p.4.
- 102 Jackson, *supra* note 9, pp. 755-63.
- 103 Kolasa, *supra* note 84, p. 31.
- 104 c.f. Jackson, *supra* note 9, p. 760. (In which he summarizes the GATT Law as follows: (1) Legal norms, backed by a complaint or a dispute-settling procedure, (2) elaborate discussion and consultation with a view to altering other nations to future national policies, (3) the use of working parties, subcommittee and discussions in plenary sessions to bring moral force upon countries to conform their individual national policies and practices to either the legal norms or the stated objectives of GATT, and (4) the use of negotiation or bargaining as a means to formulate new obligation and alter differences about old obligations.
- 105 GATT, Article 28 bis(2)(a).
- 106 GATT Article 10 concerning "publication and administration of national trade regulations".
- 107 Unlike reciprocal concessions, benefits or privileges granted under GSP system can be withdrawn unilaterally without given prior notice and consultation, because they are given in one-way direction and on a non-reciprocal basis.
- 108 Castel, *International Business Transactions* (1986), p. 41.
- 109 Stone, *supra* note 22 p. 13.
- 110 As to functions of GATT, see Stone, *supra* note 22, pp. 43-45.
- 111 GATT, Article 34.

- 112 Dam, *supra* note 9, p. 318; Jackson, *supra* note 9, p. 1179.
- 113 Kostecki, *supra* note 16, pp. 43-51, 65-70, 72-73, 79-83.
- 114 See E. Patterson, "Improving GATT Rules for Nonmarket Economies" 20 *J.W.T.L.* 185.
- 115 Jackson and Davey, *supra* note 4, p. 1179.
- 116 Dam, *supra* note 9, p. 318.
- 117 G. & V. Curzon, "GATT: Traders' Club" in Robert Cox et al (eds), *The Anatomy of Influence* (Yale University Press, 1973).
- 118 Most East European countries believed in Marxism, which essence is that capitalism is doomed by its exploitive nature, and predicted that the capitalist world would undergo another more devastating economic crisis than the pre-war Great Depression. For detailed discussion see Kostecki, *supra* note 16, pp. 3-6.
- 119 *Id.* p. 1.
- 120 *Id.* p. 3.
- 121 *Id.* p. 4.
- 122 *Id.* pp. 5-6.
- 123 *Id.* p. 5.
- 124 *Id.*
- 125 *Id.* pp. 4-5. Both the Soviet and Eastern Europe argued that non-discrimination should not restrain any country from determining the form of its economic relations in its own best interest, and bilateralism did not conflict with their understanding of non-discrimination, instead, it could turn out to be an effective weapon countries were important exporters of certain raw materials in great demand in world markets.
- 126 *Id.* pp. 9-10.
- 127 *Id.* p. 4.
- 128 The doctrine which is deemed as a major advance in post-war East-West relationship has been widely accepted by almost all socialist countries as one of the major principles of international law in their foreign relations to the West counterpart since its inception.

- 129 Kostecki, *supra* note 16, pp. 10-14.
- 130 GATT Doc. MGT/81/58, Aug. 1958 and ADD. 1, Oct. 1958.
- 131 GATT Doc. L/3050, Aug. 1968, p.1.
- 132 For detailed discussion, see Kostecki, *supra* note 16, pp. 27-30, 93-97.
- 133 GATT Doc. Spec. (1971).
- 134 M. Kostecki, "Hungary and GATT", *J.W.T.L.* (1974) pp.401-19.
- 135 Kostecki, *supra* note 16, pp.31-32.
- 136 With respect to Hungarian reciprocity formula, see Kostecki, *id*, pp. 97-98.
- 137 *Id.* pp. 25-27.
- 138 Gregory and Stuart, *supra* note 53, pp. 286-296. Re: "Yugoslavia: Market Socialism".
- 139 See GATT BSID, 8th Supp., 1960, p. 18.
- 140 Evolution of the Yugoslav foreign trade system is discussed by H. Matejka, "Foreign Trade Systems", In Hans-H. Hohman, Michael Kaser, Kare Thalheim (eds), *The New Economic Systems of Eastern Europe* (London: Oxford University Press, 1975), pp. 468-73.
- 141 GATT BISD, 14th supp., 1966, pp. 49-59.
- 142 *Id.*
- 143 GATT BISD Vol. II, p. 36.
- 144 *Id.* The U.S. Congress accepted the Trade Agreement Extension Act requiring withdrawal of MFN treatment in trade with the "communist-dominated countries".
- 145 Grzybowski, "Socialist Countries in GATT" 28 *J.W.T.L.* 539, 543; E. Patterson, "Improving GATT Rules for Nonmarket Economies" 20 *J.W.T.L.* 185, at 204.

- 146 See GATT Doc. C/M/160, at 2 (Sept. 24, 1982); GATT Doc. C/M/173, at 2 (Nov. 16, 1983). As "observers", non-member nations can attend the annual sessions of the CPs, but may not vote on any issues raised. See GATT Rule of Procedure For Sessions of the Contracting Parties 8, reprinted in GATT BISD, 11 (12th Supp. 1964). China formally notified the Director General of the GATT that China wishes to rejoin the GATT on July 10, 1986. see GATT Doc. L/6017 (July 14, 1986).
- 147 See *Trade in Textiles*, BISD, *id.*, pp. 293, 294-97. China formally became observer in 1984. See GATT Doc. L/5712 (Oct. 26, 1984).
- 148 K.C. Kennedy, "The Accession of the Soviet Union to GATT" 21 *J.W.T.L.* 23, (1987); Note, "Soviet 'Participation' in GATT: A Case for Accession", 20 *N.Y.U.J. of Int'l Law & Politics* 477 (Winter 1988).
- 149 *Id.*
- 150 Kostecki, *supra* note 16, pp. 109-10.
- 151 *Id.*, pp. 100-104.
- 152 *Id.*, p. 134.
- 153 R. Herzstein, "China and The GATT: Legal and Policy Issues raised By China's Participation In the General Agreement On Tariffs and Trade" 18 *Law & Policy in Int'l Business* 371, pp. 385-92.
- 154 See R. Carbaugh, *International Economics* 180 (1985).
- 155 *Id.*, p. 183. See *Carbon Steel Wire from Poland*; Final Negative CVD Determination. 49 Fed. Reg. 19374, 19375 (Dep't Comm. 1984) (hereinafter *Carbon Steel Wire from Poland*).
- 156 Plans in NME are set by state planning commission and other local authorities. See Kennedy, *supra* note 148, pp. 25-26.
- 157 Conn, "A Comparison of Alternative Incentive Structures for Centrally Planned Economic Systems" 3 *J. Comp. Econ.* 261, 262 (1972).
- 158 *Carbon Steel Wire from Poland*, *supra* note 155, 19370. 6 ITRD 1176, ITA (Final, 1984).
- 159 Dam, *supra* note 9, p. 318.

- 160 NME countries usually mark up the price of imported goods to limit or control the volume of imports. See Kostecki, *supra* note 16, pp. 57-58, 79-81.
- 161 Dam, *supra* note 3, p. 318.
- 162 *Id.*, pp. 318-19.
- 163 *Id.*, p. 319.
- 164 Since all of the NMEs' currencies are not freely convertible, transactions have to be subject to exchange controls. There exist virtually no facilities for mutual clearing of accounts with FMEs. Dam, *id.*, p.319.
- 165 J. Spero, *The Politics of International Economic Relations* 360-61 (1985).
- 166 Dam, *supra* note 3, p. 319.
- 167 *Id.* p. 320.
- 168 Incentive system in foreign trade is such that foreign trade organizations or corporations can retain certain sum of foreign currency, their employees can earn bonus, if the volume of trade with FME countries meets or exceeds the state-determined target or plan. see K. Kennedy, *supra* note 1157, p. 26; also R. Lipsey & P. Steiner, *Economics* 803 (1969).
- 169 Gregory and Stuart, *supra* note 53, pp. 284-318. (discussing variants of socialism).
- 170 Kostecki, *supra* note 16, pp. 46-47.
- 171 See Bialer & Afferica, "The Genesis of Gorbachev,s World", 64 *Foreign Affairs*. 605. Where the authors have identified seven reform measures undertaken or contemplated by the Gorbachev's cabinet: "wholesale change in managerial and administrative personnel and their reduction; increase in labour discipline; diminution of the number of indicators in central planning and greater stress on quality and costs; technological progress; agricultural improvement; development of infrastructure; education; and effective utilization of the Soviet strong point, centralized mobilization of resources for essential goals." *Ibid.* p. 615.
- 172 Kostecki, "State Trading By the Advanced and Developing Countries: The Background", pp. 6-21. in *State Trading in International Markets* (Kostecki ed. 1982)

- 173 See Comment, "Air Bus and Its Ilk: Turning Nose at GATT"
29 *Harv. Int'l L.J.* 111 (Winter, 1988), 115-19.
- 174 Stone, *supra* note 22, pp. 173-74.
- 175 See Y. Narita, "Administrative Guidance" (1968) 2 *Law in Japan: An Annual* 586; K. Yamanouchi, "Administrative Guidance and the Rule of Law" (1979) 7 *Law in Japan: An Annual* 22.
- 176 Oystein Noreng, "State Trading and the Politics of Oil" pp. 103-116. in *State Trading In International Markets* (Kostecki ed. 1982).

P A R T T H R E EFUNDAMENTAL RULES OF GATT: COMPATIBLE WITH NME SYSTEM?

Beyond conflicting ideologies reflected in market and non-market economies, a number of fundamental rules of GATT seem to be incompatible with NMEs. This chapter is devoted to discussing how GATT antidumping rules can be applied to exports from a NME when there is no freely determined price in that economy to which the export price can be compared. It will also discuss the application of rules against subsidies and use of quantitative restrictions (QRs) to a NME where a government agency determines import and export levels in advance and where government control permeates the economy. Additionally, whether tariff negotiations between free-market economies and NMEs can be meaningful if import levels are determined not by tariffs but by economic plans will also be considered. However, the focus of the discussion is on the compatibility of NME's state trading system with GATT major rules.

All these questions are of practical importance when major trading partners apply GATT rules to a NME country. All these questions are crucial when integrating the NME into GATT framework and ought to be examined in a reversed order starting with a rule-by-rule approach. Considering the scope of the thesis, the examination is limited only to some major GATT rules.

3.1. GATT RULES ON STATE TRADING AND NME

3.1(1) GATT RULES ON STATE TRADING

GATT rules on state trading are enunciated in its Art. 17. The focus of Art. 17 is non-discrimination and commercial criteria in international trading. The Article states:

"[S]uch enterprise shall in its purchases or sales involving either imports or exports, act in a manner consistent with the general principles of non-discriminatory treatment prescribed in this Agreement for government measures affecting imports or exports by private traders."¹

It goes on to require that:

"[S]uch enterprises shall...make any such purchases or sales solely in accordance with commercial considerations, including price, quality, availability, marketability, transportation and other conditions of purchase or sale, and shall afford the enterprises of the other contracting parties adequate opportunity...to compete for participation in such purchases or sales."²

Clearly, the original intent of GATT is to minimize the potentials of state trading practices. While recognizing that state trading can be used as an instrument of trade control policy, GATT also recognizes that state trading often presents serious obstacles to trade expansion.

The 1957 Amendments to GATT reiterated this position and identified two main reasons that might lead to serious obstacles to the expansion of international trade. They are:

(1) state trading might be served as "a substitute for QRS,

tariffs and subsidies;³ and (2) special privileges granted to a trader by the state might result in a monopoly situation.⁴ This is because functional equivalent of taxes or subsidies may be implemented through the determination of the differential between external prices and the domestic resale prices for imports or domestic purchase price for exports. The functional equivalent of QRs may be implemented through the determination of quantities imported or exported. Furthermore, a policy of discrimination may be implemented through the determination of the source of imports or the destination of exports. Based on these grounds, Article 17 together with the supplementary provisions of Art. 2(4) endeavors to minimize the potentials of state trading practices.

Despite being a trade barrier, state trading is not prohibited by the provisions of GATT. It is admissible as long as it is operated "in a manner consistent with the general principle of non-discriminatory treatment",⁵ and according to the commercial considerations rather than political or other non-commercial criteria.⁶

Art. 3(4), Art. 2(4) and an interpretive note of Art. 2(4) seem to be relevant in regulating state trading practices. Art. 3(4) indicates that non-discrimination is not only achieved by MFN treatment, but also by national treatment which shall be accorded to foreign imports after they enter a CP's domestic markets. A proper understanding of non-discriminatory requirements in this regard helps to clarify the issue as to whether the nondiscriminatory treatment

requirement coupled with the "commercial considerations" standard, means non-discrimination among foreign sources of supply (MFN treatment) or non-discrimination against foreign sources in favor of domestic sources (national treatment).

Also, Article 2(4) provides that any import monopoly maintained by a contracting party:

"shall not...operate so as to afford protection on the average in excess of the amount of protection provided for in that Schedule."⁷

In other words, a contracting party shall not use state trading monopoly to accord, in the case of bound items, protection to domestic production beyond that provided for in its negotiated tariff schedule.⁸

Also, the interpretive note of Art. 2(4) guides contracting parties in applying Article 2(4):

"except where otherwise specifically agreed between the contracting parties which initially negotiated the concession...in the light of the provisions of Article 31 of the Havana Charter."⁹

Article 31 of the Havana Charter requires each member of the ITO maintaining an import monopoly to negotiate upon request of another member for the reduction of the protection to domestic production afforded by that monopoly. This requirement was eventually omitted from GATT Article 17.¹⁰ Thus the interpretive note does not impose on contracting parties a duty to negotiate with respect to products subject to import monopolies.¹¹

The thrust of GATT Art. 17 is to minimize but not to prohibit state trading operations. Nevertheless, GATT fails to provide a clearly articulated definition of state trading

enterprises in the first place. It merely states that state trading occurs when a contracting party "establishes or maintains a State enterprise wherever located, or grants to any enterprise, formally or in effect, exclusive or special privileges".¹² Assuming this is the definition of STEs, one can find no guidelines as to what constitutes "exclusive or special privileges". This ambiguity has resulted in heated debates among economists, centering around the functional characteristics of state trading and optimal mode of desirable international coordination and regulation. The provision leaves the door open for signatories to interpret it according to their own criteria and understanding.¹³

Despite the controversies the criterion of direct government control has most frequently been used to define STEs.¹⁴ Consequently, STEs are classified into three categories: (1) state owned enterprises; (2) state controlled enterprises; (3) privileged enterprises.¹⁵ If Government gives an enterprise operational criteria or central directives or grants monopoly, such an enterprise may be defined as a STE. Accordingly, there are three categories of agencies: (1) state trading agencies, (2) regulated agencies, and (3) mixed agencies.¹⁶

Functionally, state trading is more invisible, flexible and thus often implemented as a substitute for tariffs, subsidies and QRs.¹⁷ It is a substitute for tariffs when implemented to protect domestic producers and improve the terms of trade. Economic analysis suggests that state trading

is often a trade policy instrument and implemented to pursue objectives of government policy.¹⁸ A comparison of state trading and private trading shows that under commonly used pricing rules¹⁹ by a state trader the instrument of state monopoly trading and *ad valorem* tariff levied on competitive private trading are equivalent.²⁰ Discriminatory state trading and a set of *ad valorem* taxes - subsidies levied on competitive private trading are also equivalent.²¹ Economic analysis also shows that any sequence of market solutions obtained by exclusive state trading under specified pricing rule and sequence achieved by competitive private trading under specified sequence of sets of *ad valorem* taxes-subsidies could be "amazingly identical."²² For these reasons the instruments of state trading and tariffs are in fact inter-replaceable or inter-changeable.²³

State trading becomes a substitute for subsidies when government agencies afford STEs special or exclusive privileges of trading with foreign partners to promote export expansions. Since the nature and function of subsidies are to grant special or exclusive privileges or favors by a government, they are mutually comparable and replaceable.

State trading is also categorized as QR when it introduces discrimination against sources of foreign imports. Because of this substitutability, GATT gingerly states that the so-prescribed QRs should include those restrictions "made effective through the operations of state trading,"²⁴ and thus

extends its general principle of non-discrimination to the state trading operations.

Tariff negotiations with NMEs often ultimately touch upon internal price levels and price structures. The dual pricing system (i.e. discriminatory prices applied to domestic manufacturers and foreign imports of like goods) often presents a major barrier for NME countries to participate actively in the tariff negotiations.²⁵ Consequently, tariff negotiations would have to be replaced by negotiations on global quota undertakings. At the same time negotiation on global quota undertakings also called import commitments was considered as a more effective approach than that on tariff concessions in dealing with the accession of NME countries to GATT because mere tariff reductions in NME countries were of limited meaning as most of NMEs maintained central planning.²⁶

3.1.(2) ARTICLE 17 AND NME

Article 17 was supposed to be applied to State trading enterprises (STEs) both in FME countries and NME countries. It had its origins in Art. 27 of the U.S. Suggested Charter,²⁷ which became Article 31 of the Havana Charter, entitled "Expansion of Trade of State Monopolies of Individual Products".²⁸ Due to the USSR and other NME countries' non-participation in the Preparatory Work for the establishment of the ITO, Article 31 was not written into the text of GATT. Article 17 therefore provides the only basis in GATT to deal

with the problem of integrating NME system into the GATT framework.²⁹

Historically, the Article was drafted only to deal with "occasional" state trading in market economies and thus has limited applicability to NME system. GATT assumed minimal government intervention in private enterprises despite the fact that the government may afford certain enterprises special or exclusive privileges in conducting import and export trade, or even engage in trade itself (typical state trading). The overwhelming requirement of Article 17 was that state trading be operated according to commercial criteria and nondiscrimination. It was thought that since state trading is an admissible and perhaps desirable form of trade control in certain circumstances, the requirement of non-discrimination could then be achieved by requiring that STEs act as if they were private enterprises aiming at maximum profits.³⁰

This assumption, however, is poorly-framed and ill-adapted to the NME countries.³¹ Considered in the context of the centrally planned state trading economies, government intervention is not rare but permeates their economic systems. The central idea and thrust of Article 17 is pronounced in its para. 1 to the effect that:

"[A state trading] enterprise shall, in its purchases or sales involving either imports or exports, act in a manner consistent with the general principles of nondiscriminatory treatment..."³²

Presumably such requirements can hardly be enforceable in NMEs since STEs in NME countries are created precisely to achieve the goals that are not normally assumed by private

enterprises. The function of STEs in NME countries is basically the same as that of government agencies. Thus the GATT's assumption that STEs should be operated as though they were private enterprises is not amenable to the circumstances of state trading problem in NMEs. The domain of its application is only limited to occasional state trading occurring in FME countries.

Generally, state trading has been classified into the following three categories: (1) occasional state trading in market economy; (2) loose state trading in NMEs (here the term NME is imprecisely used only to reflect their traditional socialist system); (3) command state trading in NMEs. The GATT requirement of nondiscrimination and commercial behavior would be applicable to occasional state trading in market economies. And once the government has granted an enterprise "exclusive or special privileges"³³, it no longer controls the activities of the enterprise.

As noted earlier, state trading can be an instrument of trade control policy just as tariffs or quantitative restrictions, it can also be a trade policy object.³⁴ It follows that: (a) If a STE is operated as an object of trade policy acting in the same manner as its private counterparts, it shall not be subject to specific provisions other than tariffs, QRs, and other general rules since the regulation has already been provided for somewhere in the GATT;³⁵ and (b) If a STE implemented to act as a trade policy instrument it would need specific regulation in the same way as other trade policy

instruments such as tariffs, QRs, subsidies.³⁶ In other words, if a STE is created as an object of government trade policy acting as if it was private trading, there will be no problem of compatibility arising with the GATT requirement of observing commercial behavior. But if a STE is created as trade policy instrument like tariffs or QRs, it should be subject to specific regulation.

The nature of state trading in NME and FME is different to the extent that NMEs' governments control STEs through central plan or target whereas FMEs' government does not control their STEs after granting them exclusive or special privileges and allows the STEs to retain certain degree of liberty in deciding for or against import in accordance with supply and demand in both domestic and international markets.

The GATT rule could also be well applied to "loose" state trading system where a STE maintains a direct link between foreign and domestic prices in purchases or sales. The government only uses tariff protection under normal conditions and the state either owns the enterprise or grants it exclusive privileges to support a monopolistic or semi-monopolistic position.³⁷ Once the privileges have been granted and monopolies established, government interference is limited only to traditional trade control measures.³⁸ This method of restricting or expanding trade through instruments such as tariffs, production subsidies and quotas under circumstances is acceptable to GATT.³⁹

In Eastern Europe, foreign trade regimes are very diversified. Hungarian and Yugoslav regimes for trade with the West may be treated as examples of loose state trading. The foreign trade system implemented in Poland, Romania, Bulgaria, Czechoslovakia seems to fall in the model of command state trading system.

China is moving towards loose state trading system as its economy has been decentralized since the inception of economic and foreign trade reforms in 1979.⁴⁰ The recent reform has decentralized the managerial authority of foreign trade so as to empower the enterprises to decide appropriate forms of conducting foreign trade and make their own decisions.⁴¹ The further reform will abolish mandatory planning or replace it with guidance planning and market regulation.⁴²

Currently, the State administers foreign trade mainly through legal and economic regulatory authorities without direct intervention in the enterprises.⁴³ The trade monopoly of STEs mainly refers to foreign trade corporations (FTCs) and is limited to some key commodities such as steel, fertilizer, cereals, timber, chemical fibers, autos, disused ships, tobacco and rubber.⁴⁴ A government agency called MOFERT supervises FTCs to implement foreign trade policies, regulations and mandatory plans (not including such directives as the source of supply or destination, price paid or asked and degree of transformation).⁴⁵ It generally does not interfere in the business activities of an FTC.⁴⁶ Also it does not set guidelines and detail rules regarding the choice of

origin of imports. The origins of imports are decided by FTCs themselves upon request of end-users and conditions of international market--though the administrative supervision cannot at present be abolished.⁴⁷

The above examination shows that STEs in China are able to carry out Art. 17 of the GATT, and fulfill "commercial considerations" standard. No country-specific restrictions are to be imposed on the imports and thus no discrimination arises against foreign sources of imports. Also, the volume or level of FTCs' imports is regulated according to market forces of supply and demand both in the domestic and international market.⁴⁸

By contrast, foreign trade in the USSR is a somewhat complete "state monopoly".⁴⁹ Under the Soviet foreign trade regime, foreign trade is conducted by the Foreign Trade Organizations (FTOs).⁵⁰ Soviet producers and manufacturers cannot conclude contracts with foreign firms without going through the appropriate FTO. FTOs are subject to the State Planning Commission and Ministry of Foreign Trade, and therefore are unable to trade with western partners according to "commercial considerations only" standard.⁵¹ Although Mr. Gorbachev has been making efforts to undertake political and economic reforms, the overriding feature of the Soviet trading system remains political rather than economical.⁵²

While the loose state trading system is acceptable to GATT, the compatibility of the command state trading system with the GATT assumption is very doubtful and ought to be

determined on individual merits. Obviously the application of the GATT non-discrimination to command state trading system requires that no country-specific target controls be introduced.⁵³ Targets in Poland and Romania were not country-specific and consequently, they could not implement discriminatory policies towards particular countries, though they did treat differently convertible and non-convertible currency areas.⁵⁴

If country-specific target controls exist in command state trading economies, tariff negotiations will be of limited use. Accordingly, negotiations on tariff concessions would have to be accompanied by negotiations on import increase commitment.⁵⁵ And the weight of negotiations on targets would have to be attached to the nondiscriminatory character of trade control measures and import targets.⁵⁶

3.1(3) CONCLUSION AND SUGGESTIONS

In sum, the GATT rule on state trading was originally only concerned with occasional state trading in market economy. It could be well applicable to "occasional" state trading in FME as well as "loose" state trading in some selected NME countries. But it would have considerable difficulty in applying this rule to those STEs established under the guidance of central plan where there is no direct link between domestic and foreign prices and where target instead of tariffs is implemented as the main element of

protection. The difficulty lies in the inherently problematic assumption of GATT itself. Quite contrary to the assumption that STEs should be established or maintained consistent with the principle of nondiscrimination and acting as if they were private trading enterprises, STEs in the NMEs with "command" state trading systems have been created just to function in a similar way to which government agencies function. The government not only grants the enterprises "exclusive or special privileges", but also controls or directs their activities from time to time through central planning or target measures. In such case it is perplexing whether the GATT requirements can be fulfilled when STEs are established precisely to achieve goals not normally assumed by private enterprises.⁵⁷ In effect, Article 17 is both unrealistic and ill adapted to NMEs with command state trading system.⁵⁸

This shortcoming of Art. 17 shows that GATT rules on state trading has limited application to NMEs especially the economies of command state trading systems.⁵⁹

Moreover, GATT normative approach to state trading is defected. Under normative approach, GATT deals with state trading as follows:

- "(i) by identifying what constitutes a STE;
- (ii) by extending nondiscriminatory MFN treatment to such STEs;
- (iii) by imposing them a duty to act according to commercial considerations only, barring the use of quantitative restrictions;
- (iv) by excluding nullification of tariff concessions through import mark-ups in the case of import monopolies."⁶⁰

The general rules articulated in Art. 17 are non-discrimination and commercial criteria. Such general rules can hardly be an efficient tool to prevent specific government measures of a discriminatory or protective nature made effective through state trading operations.⁶¹ This is because state trading operations are very flexible, invisible or non-transparent.⁶² By using this approach, trade liberalization can rarely be achieved because it only addresses a process that escapes detailed regulation and close surveillance.⁶³ Deviation from the commercial consideration standard can hardly be detected. Also, the information necessary to survey the application of the standard is rarely disclosed.⁶⁴ What GATT rules can do is to state basic standards such as the non-discrimination and commercial criteria to be observed.⁶⁵

In addition, the result-oriented approach also known as import commitment approach is flawed. Although the approach is designed to overcome the difficulties to which the normative approach gives rise (i.e. to make the obligations clear and compliance easily detectable), it is gravely unsatisfactory for the reasons that: (1) commitments undertakers have no quantity assurance that they are not being discriminated against; and (2) import requirements can hardly be precisely determined in advance. Consequently, a minimum import commitment can easily become either superfluous or distorting.⁶⁶ Furthermore, the "fair share" approach which was employed to deal with Eastern bloc's integration problem is "more political than economical in nature."⁶⁷

Accordingly, a revision of the GATT rules and approaches is required. The revision can be undertaken along the line of material injury approach which deals with subsidies. It is observed that:

"[I]f state trading is accepted as an alternative method of intervention of states in economic matters, its treatment should remain basically consistent with that granted by the GATT to other methods of intervention, as used in the case of subsidies."⁶⁸

"Subsidy" and state trading are analogous as regards being used as instruments of trade controls. GATT recognizes that they both will be obstacles to the expansion of international trade owing to their "injurious effects" which are similar in nature.⁶⁹ Therefore, a solution along the lines of the "material injury" philosophy adopted in the Subsidies code and antidumping code would appear "logical".⁷⁰

GATT is neutral as to the ownership of enterprises.⁷¹ What matters are the modes of government control over enterprises. GATT rules on state trading are directed towards state-controlled enterprises.⁷² GATT assumes that governments control the operations of STEs mainly through "general rules" such as rules on import tariffs, QRs and subsidies, and thus regulate primarily the use of such policy instruments.⁷³ However, GATT recognizes that governments control trade also through "specific measures" made effective through the operations of state-trading enterprises.⁷⁴ Thus it subjects those enterprises to special requirements designed to ensure that they are not used to circumvent the rules on general policy instruments, and to minimize the potential of

such operations which will create serious obstacle to the expansion of international trade.⁷⁵

3.2 NON-DISCRIMINATORY ADMINISTRATION OF QRS AND NMES

3.2(1) GATT RULES ON QRS

Quantitative restrictions (QRs) normally refer to restricting or expanding foreign trade by quantitative specifications.⁷⁶ They are applied most frequently by means of quotas and licenses.⁷⁷ GATT recognizes that QRs often constitute obstacles or barriers to international trade and thus explicitly forbids the use of such trade controls unless in special or exceptional circumstances as permitted by it.⁷⁸

While quota undertaking is an admissible term of trade in special circumstances, it should generally be non-discriminatory in nature towards foreign sellers or exporters.⁷⁹ Para. 2 of Article 13 applicable to NMES requires that:

"quotas representing the total amount of permitted imports (whether allocated among supplying countries or not) shall be fixed..."⁸⁰

And contracting parties shall not require that:

"import licenses or permits be utilized for the importation of the product concerned from a particular country or source."⁸¹

These requirements aim at dismantling import quotas or licenses with individual or country-specific nature. QRs should be administered on nondiscriminatory basis and be

applied to all GATT members.⁸² This obligation is also extended to those restrictions "made effective through state trading operations."⁸³

Quotas should be allocated globally rather than to specific countries or sellers. The reason for this requirement is that in a general way, the more specific the direct allocation (i.e. the more rigidly fixed the direction of export and source of import), the greater the danger of country discrimination.⁸⁴ However, if specific allocation of importation of a particular product is desired, the countries exporting the product should seek an agreement on the allocation of shares in the quota.⁸⁵ Such agreement must take into account commercial considerations such as "changes in the terms of trade, QRs, excessive tariffs and subsidies".⁸⁶

Likewise, GATT intends contracting parties not to specify countries or source of import in their licences but to apply global licences rather than individual licences.⁸⁷ Individual licences are permitted only for the purpose of handling specific quotas.⁸⁸ It is the duty of the GATT members maintaining quotas and licences to provide information and allow consultation with regard to this form of trade control.⁸⁹ Such information should indicate the administration of the licensing system, past licences issued and the allocation of licences.⁹⁰

In addition, as clearly stated in an interpretive note, restrictions "made effective through state trading operation" should also be generally eliminated.⁹¹ However, no explicit

criteria of non-discrimination have been formulated for this type of QRs.⁹² Moreover, the information requirement imposed on using quotas and licences is not imposed on QRs made effective through state trading operation.⁹³ Nonetheless, it is clear that the original purpose of the GATT rules is to submit the QRs implemented through state trading links to the same general principle of non-discrimination affecting other QRs.⁹⁴

3.2(2) ARE NMES COMPATIBLE WITH NON-DISCRIMINATORY USE OF QRs?

In Eastern bloc countries foreign trade is subject either to global or individual licences.⁹⁵ In Hungary, the majority of imports, both from NMES and FMEs are transacted under global licences which are more commodity-specific rather than country-specific.⁹⁶ Conversely, in Poland and Romania the licensing systems are based, to a large extent, on individual licences which are more country-specific for trade with NMES than for trade with FMEs.⁹⁷ Although the Hungarian licensing system is basically compatible with the GATT requirement, Hungary's accession to the GATT did not solve the discrimination problem between quotas issued for CMEA countries and for FME countries.⁹⁸ Additionally, Hungarian quotas contained protective elements that would draw special attention to its GATT trading partners.⁹⁹

In China the import licensing system is administered by MOFERT on a global basis without quota.¹⁰⁰ It is not country-

specific but commodity-specific.¹⁰¹ Although the import of some commodities under mandatory planning is subject to restrictions in total volume, it is not allocated among supplying countries.¹⁰² The government does not grant special or exclusive privileges to foreign trade corporations (so-called STEs) as regards their applications for import licences. The government does not deny any other enterprises the right to import a certain product by not granting approval to import that product or to acquire the necessary licence unless the imports of the commodities are prohibited by State Regulations.¹⁰³ The criteria for import restrictions in China are based on supply and demand conditions, domestic production and foreign exchange earnings.¹⁰⁴ As expressed in the Chinese government "Questions & Replies", "the purpose of the import licensing system is simply to regulate, not to prohibit the imports."¹⁰⁵ Therefore, the Chinese licensing system may well be compatible with the GATT requirements.

In summary, GATT rules on non-discriminatory administration of QRs may well be applied to the state trading system functioning only through state trading links such as Hungary, Romania and China. However, if the GATT is to regulate the command state trading system such as Poland, Romania and the Soviet Union, detailed explicit criteria of non-discrimination must be enumerated and information requirements be attached to those criteria.

3.3. TARIFF PROTECTION V. TARGET PROTECTION

The GATT-based multilateral trade order assumes a direct link between foreign and domestic prices. Once foreign goods enter a CP's territory, the CP shall not mark up the original price of imports unless for customs or excise tax reasons. This promotes fair and free competition in international trade. GATT expects its members to control trade indirectly through prices and tariffs rather than through direct trade control instruments (licensing quotas) as discussed earlier. Tariffs in the GATT are presumed to be the main economic lever regulating import and export and the key protective element.¹⁰⁶ This is because by using tariffs as protection protectionist elements are easily identified and become more visible and less discriminatory in nature.¹⁰⁷ Based on this assumption, GATT in its Article 11(1) requires that protection be afforded to domestic producers exclusively through the customs tariffs.¹⁰⁸

Therefore the use of tariff instrument is an important aspect of participation in the GATT. And the reconciliation and integration of NMEs into the GATT should also be focused on tariffs. This requirement can easily be fulfilled under the loose state trading system. A tariff-protected state trading system (occasional state trading) can conform to GATT standards and undertake meaningful obligations regarding the ceiling of nominal tariff protection and non-

discrimination.¹⁰⁹ Negotiations on reciprocal reduction of protection can use the "symmetric reciprocity formula."¹¹⁰

The formula provides equivalent concessions made by each participant whose economy is basically tariff protected. However, as for participation of command state trading system in the GATT, this formula would be less effective. Kostecki pointed out that:

"the central role of the customs tariff as an instrument of a country's participation in the GATT may raise some difficulties in applying the GATT provisions to the state-trading systems...which relies on plan targets".¹¹¹

Tariffs in such trading system may only be used as a supplementary instrument of protection to subsidies, QRs and government control over trade, etc.¹¹² That implies that negotiations on reciprocal reduction of protection between tariff-protected economies and state trading economies maintaining multi-commodity or single-commodity import targets would require an "asymmetric reciprocity formula".¹¹³

Since the key ingredient of the GATT requirement is that tariffs be used as the only protective element in regulating import and export trade, our focus of examination is on evaluating what kind of roles tariffs play under above classified two types of state trading systems.¹¹⁴ The role that tariffs play determines whether there is a direct link between domestic prices and foreign prices of imported goods, and whether there is a mark up of import prices. The element of whether there is a direct link between domestic prices and foreign prices in turn determines the compatibility of state

trading systems with the GATT tariff protected requirement. If a state trading system is established to eliminate or limit the direct linkage between domestic prices and foreign prices, it is incompatible with the GATT requirement. If, however, a state trading system is to maintain such linkage and use tariffs as a main economic lever influencing import and export trade, it complies with the GATT provisions.¹¹⁵

When Poland and Romania acceded to the GATT they were unable to establish such a link. Tariffs were not a chief instrument influencing level of trade. Instead, variety of protective and discriminatory measures were employed to restrict foreign imports.¹¹⁶ Hungary, on the other hand, due to its economic and trade reform, made efforts to remove unnecessary barriers to trade, aiming at using tariffs as a main force to balance imports and exports. Its tariff system was generally conformed with the non-discriminatory requirements of the GATT though such exceptional practices as using custom quotas, permit-slip procedure and the suspension of tariff rates remained unsatisfactory to the GATT countries.¹¹⁷

In China the general policy of the Customs tariff is to carry out the "open door" policy, to encourage the exports, to promote the imports of necessities and to protect and improve the development of the national economy.¹¹⁸ Influencing the level of trade is a primary policy objective while revenue is only a secondary consideration.¹¹⁹ Currently, there is no separate legislation in China providing relief to domestic

producers from injurious imports.¹²⁰ This suggests that China will get involved in the future negotiations on tariff reduction and concessions. China has expressed its view of taking into full consideration the appropriate tariff concession as an obligation for resuming its status as a contracting party to GATT on the one hand and the protection of domestic industry on the other.¹²¹ For the purposes of customs valuation, the criterion adopted in the Chinese rules of origin is "substantial transformation".¹²²

Chinese Customs also levy an "import regulatory tax" on certain goods for the purpose of protecting domestic industry.¹²³ Although it is applied to all foreign imports, it affords a relative preference to domestic goods and thus is incompatible with "national treatment" of GATT Article 3.¹²⁴

3.4 DOMESTIC PRICE FORMATION: DUMPING OR SUBSIDIES?

GATT requires its members to establish a direct link between domestic and foreign prices and not to dump goods by sale at less than fair value (normal value). Domestic price formation is closely related to dumping.¹²⁵ GATT provisions may be fully applicable to loose state trading economies whose price formation conforms with GATT standards. But, GATT rules on dumping may make little or no sense when applied to NMEs maintaining command state trading.¹²⁶ The GATT does not prohibit domestic maximum price control. The core of its provision is to call for those who apply internal price controls to take into account the interests of exporting

contracting parties with a view to avoiding to the fullest practicable extent any prejudicial effects.¹²⁷ In essence, foreign exports should be accorded "national treatment".¹²⁸ And domestic price control should not result in an increase in protection above the level agreed upon by the GATT countries in tariff schedules.¹²⁹ This so-called "consolidation" provision also applies in the case of import monopoly.¹³⁰ One could imagine that the GATT rules on domestic price formation make sense only in market economies or economies maintaining loose state trading systems in which there is a direct link between domestic and foreign prices.¹³¹ They have little meaning as applied to nonmarket economies maintaining command state trading where there is little or no link between domestic and foreign prices.¹³²

In Poland and Romania, domestic prices were centrally fixed by central or local authorities. The prices were generally based on average costs excluding interest.¹³³ Considering resource allocation and the requirements of intensive economic growth, these prices were not rational in terms of supply and demand.¹³⁴ The allocative function of price formation within the limits of the obligatory targets in the foreign trade sector was of little practical significance to GATT due to the maintaining of targets, individual licensing and the existence of the equalization mechanism.¹³⁵ There existed duality of the price system: on average, consumer prices were higher than producer prices even for the same or similar products.¹³⁶ The prices of essential products

were much lower than that of light industrial and luxury items. Prices of imported goods were fixed too high to be purchasable by the domestic consumers.¹³⁷

Unlike Romania and Poland, Hungary commenced its reform in economic and foreign trade structure in 1969 and the reform paved the way for market relationships among domestic enterprises and prices assumed an allocative function.¹³⁸ In Hungary, prices have been categorized into three: fixed prices; prices adjusted in conformity with official regulations; and free market prices.¹³⁹ The Hungarian price system assured a close tie between domestic and foreign prices.¹⁴⁰ However, the automatic link of domestic and western prices remain somewhat restricted by the use of quotas, licensing and targets. Additionally, certain level of discrimination between the two prices still existed.¹⁴¹

Like in Hungary, three different prices presently co-exist in China as a result of the reform in pricing system: state fixed price, state guidance price and market-regulated price.¹⁴² The reform has shaken the previous rigid method of state fixing import and export price. Enterprises *per se* are allowed to determine prices of imports according to conditions in marketplace.¹⁴³ In determining the domestic price of an import commodity the enterprise takes into account the c.i.f. value, import duty, internal taxes, banking charges, commissions, and the enterprise assumes direct responsibility for all the profits and losses.¹⁴⁴ But for some key import products such as steel, fertilizers and grains which have an

important bearing on the national economy, their domestic prices are set by the State and the State assumes responsibility for all the profits and losses therefrom.¹⁴⁵ On the other hand, the price of an export product exported by foreign trade corporations on a commission basis is basically determined on the basis of domestic costs and international market conditions.¹⁴⁶ The prices of export products by foreign trade corporations on their own or jointly with producers, are calculated by including purchased value or production costs, transportation expenses, storage expenses, banking charges, export duty (when levied) and reasonable profit margin etc.¹⁴⁷

Generally, China has made efforts to remove unnecessary price discrimination between domestic and foreign goods. Prices in China are reflecting supply and demand. A limited link between domestic and foreign prices seems to be established. To some extent China is able to fulfill the GATT requirements.

In the USSR, however, there is no direct link between domestic prices and prices of imported goods.¹⁴⁸ Prices of imports are, for the most part, fixed by the state.¹⁴⁹ The STEs - in USSR known as "Foreign Trade Organizations" have a very limited role in determining the prices of their imported or exported goods.¹⁵⁰ Their choice in selecting sources of imports are guided by planned targets relying heavily on political considerations rather than on pure economic demand.¹⁵¹

3.4(1) GATT ANTIDUMPING AND COUNTERVAILING DUTY LAW AND
NME

As noted earlier, the assumption of GATT concerning price competition requires that its member countries establish a direct link between domestic prices and prices of foreign imports, and not to dump goods for exportation by sale at less than "normal" or fair value. As a matter of fact, domestic price formation of exporting and importing products is closely related to dumping and subsidy. Sales of exported products to another country at less than "normal value" constitute dumping within the meaning of GATT Article 6¹⁵² and may cause or threaten to cause material injury to domestic industries of the importing countries.¹⁵³ On the other hand, low pricing of export products may give special preferences to domestic producers and thus constitute subsidies.

GATT Article 6 (known as "Track I") condemns dumping and authorizes the CPs to impose antidumping and countervailing duty to equalize competitive conditions that have been distorted by dumped or subsidized imports.¹⁵⁴ The authorization is, however, given only to those CPs whose domestic industries producing like goods have suffered material injury.¹⁵⁵ Mere injury is insufficient to impose antidumping or countervailing duty but the distinction between mere injury and material injury has been always difficult to draw.¹⁵⁶ Since the primary objective of Track I is to set off the injurious effects caused by subsidized/dumped imports, the amount of antidumping duty or countervailing duty shall not

exceed the "dumping margin"¹⁵⁷ or the estimated bounty or subsidy granted.¹⁵⁸ The alleged dumped or subsidized imports can only be levied either antidumping duty or countervailing duty.¹⁵⁹

In addition to Track I, GATT Article 16 (referred to as "Track II") prohibits export subsidy on non-primary products,¹⁶⁰ with leniency for subsidies on the export of primary products.¹⁶¹ Although non-export subsidies are exempted from this general prohibition, the subsidizing country shall notify the Contracting Parties of the extent and the nature of subsidization, of the estimated effect of the subsidization on the quantity of the affected product or products imported into or exported from its territory and of the circumstances making the subsidization necessary.¹⁶²

With respect to subsidies, GATT is generally against both production subsidies and export subsidies. Although it does not forbid subsidies as such, it subjects their use to certain limits and requirements. GATT Art. 16 imposes on subsidizing CPs three types of obligations as follows:

(1) Any subsidizing CP is required to give CONTRACTING PARTIES notification on any subsidy which influences the level of trade;¹⁶³

(2) Although developing countries may use subsidies on the export of primary products, they shall not apply such subsidies in a manner which results in that contracting party having more than an equitable share of world export trade in that product;¹⁶⁴

(3) A third obligation--to cease export subsidies on any non-primary products--applies to a small group of developed CPs. No newly acceding CPs (under Art. 33) are bound by it unless they sign the relevant declaration.¹⁶⁵

3.4(2) PROBLEM OF DUMPING AND SUBSIDIES WITH NMES

Although GATT does not prohibit subsidies, members are permitted to use countervailing duty against subsidized products if they cause material injury to a member's domestic industry.¹⁶⁶ As far as the state trading systems are concerned, subsidy is considered by GATT countries to be an effective instrument of trade control, a means of increasing exports.¹⁶⁷

Under target-protected economies, subsidy is nearly indistinguishable from equalization payment (which is an import subsidy under a plan target but not in the GATT sense).¹⁶⁸ Under one-commodity target, the level of exports is determined directly and the eventual negative tax paid to the foreign trade unit is the result of a given export performance. But under multi-commodity target, subsidies could be used to influence the level of trade within the target framework and the operation of plan targets may require an equalization system.¹⁶⁹ It would be crucial to have an information network to determine whether or not there is a subsidy.¹⁷⁰

The GATT rules against dumping and subsidies have been implemented by an Antidumping Code and Subsidies Code which are signed by most of the participating countries at the Tokyo Round negotiations on tariffs and trade (referred to as MTN Codes). In the two Codes guidelines have been given as to how to interpret the confusing concept of dumping, subsidization, "domestic industry", and general criteria to determine "material injury". Regrettably, the two Codes only accord signatories a general framework. Much of the interpretive work remains at each signatory's discretion.

The philosophy underlying the GATT rules against dumping and subsidies is free market principles which promote maximum market efficiency achieved when free trade allows each country to specialize by exporting those goods it can produce most efficiently and importing those goods that it can produce only at a higher cost.¹⁷¹ The foremost objective of GATT antidumping and countervailing duty rules is to increase competition by remedying injurious effects resulting from twisted unfair pricing or trade practices.¹⁷² The overriding approach of GATT is to define whether or not the alleged imports are causing or have caused material injury to the domestic producers of like products.¹⁷³ In doing so a causal link between material injury and dumped/subsidized imports must be firmly established. And cumulation of imports as a cause of injury especially in invoking - "escape clause" under Article 19 in the circumstances of increased imports may be appropriately assessed.¹⁷⁴

The GATT rules against dumping /subsidies incorporated into the two Codes are further implemented by the Codes' signatories as foremost components of their domestic unfair trade relief laws and measures attempting to equalize competitive conditions before distorted by dumped or subsidized imports.¹⁷⁵

The above described GATT rules against dumping/export subsidies may be well applied to loose state trading economies whose price formation conforms with the GATT standards.¹⁷⁶ But still the GATT rules when applied to NMEs maintaining command state trading may make little or no sense.¹⁷⁷ The reason is that these rules are formulated along the line of freemarket principles. The major difficulty for GATT trading countries in applying the GATT rules to NMEs centers on whether the free market principles can be translated and applied to NMEs.

In any event, the GATT rules *per se* does not exempt the application to NMEs as long as NME countries remain with the GATT organization. The principal difficulty lies in determining the "normal value" of NME imports, and accurately identifying and quantifying subsidies in the absence of market-based prices, costs, and exchange rates.¹⁷⁸ In a FME prices and resource-allocation are determined by the natural forces of supply and demand and scarcity of commodities.¹⁷⁹ In the absence of government intervention, these forces interact to allocate resources efficiently to their most valuable uses.¹⁸⁰ But in a NME profits, prices and resource-allocation are controlled by the state and do not reflect the forces of

supply and demand or allocative efficiency.¹⁸¹ The price of a commodity is but one of the policy tools used by the government to promote its social, political and economic objectives.¹⁸² Prices used to determine profits need not reflect the actual costs of production because the goal of micro-economic efficiency generally does not exist in a NME.¹⁸³ Furthermore, in most NME countries there is no reliable exchange rate by which to convert the NME currency into dollars.¹⁸⁴

Accommodations have been made as to how to determine the normal value of NME imports so as to calculate the dumping margin. This has been done through the use of constructed value of a third market country approach or so-called "surrogate country" approach.¹⁸⁵ In the U.S. Congress made efforts to bridge the gap between FME and NMEs through so-called "surrogate country" approach to determine the normal value of NME imports and rendered the antidumping laws applicable to NMEs.¹⁸⁶

However, the problem of identifying and quantifying the subsidies alleged against NME has been unresolved.¹⁸⁷ This dilemma has been encountered by the U.S. Department of Commerce.¹⁸⁸ Since U.S. is one of the most important signatories to the Codes, it is helpful to use U.S. trade laws and approaches in this area as an example of how the GATT rules have been interpreted.

In the U.S. the traditional view of Commerce concerning the application of U.S. countervailing duty laws (CVD laws) to

NMEs is negative. The Commerce's view was first addressed in the case filed by a group of U.S. textile manufacturers and unions against imports from NME China alleging that China's policy of granting a preferred monetary exchange and other benefits to the producers of exported goods constituted a countervailable subsidy.¹⁸⁹ The position is more clearly disclosed in a case concerning Carbon Steel Wire Rod from Poland and Czechoslovakia¹⁹⁰ in which Commerce Department contended that a NME "[by] market standards...is riddled with distortions",¹⁹¹ where the state and the producers are virtually the same and an alleged act of subsidization is conceptually inseparable from the state's normal role of allocating resources.¹⁹² These distortions make the task of identifying and quantifying subsidies in NMEs hopeless. The contention received support from the Court of Appeals for the Federal Circuit in a landmark case of Georgetown Steel Corp. v. United States.¹⁹³ The court held that a countervailable subsidy cannot be found in a NME¹⁹⁴ and that subsidization is merely a market phenomenon that by its very definition cannot exist in a non-market economy.¹⁹⁵

However, in 1987, several bills were introduced in the House and Senate to invalidate the verdict of Georgetown Steel and apply the CVD laws against NME countries.¹⁹⁶ Of these bills one of the most successful is Section 157 of 1987 Trade Bill, which suggests the use of "surrogate" approach to circumvent the implementation problem of identifying and

quantifying subsidies in the absence of market-based prices, costs, and exchange rates.¹⁹⁷

However, as economic analysis shows that dumping and subsidies in NMEs are virtually indistinguishable,¹⁹⁸ applying both laws to NMEs would appear meaningless.¹⁹⁹ Now that antidumping duty laws have already been applied to the NMEs, CVD laws are unnecessary to be applied in this context. Efforts to apply CVD laws to NMEs are misguided and should be abandoned.²⁰⁰

It is often claimed in Western countries that NMEs tend to dump their goods on Western markets. This is because their STEs are based on discriminatory monopoly power without competitors. The prices they determine do not reflect the market forces of supply and demand. Rather they are implemented instruments of government policy resulting in long term dumping.²⁰¹ Moreover, NMEs' foreign trade often lacks flexibility in the context of changing prices and domestic production cost which in turn increases the risk of short-term dumping on Western markets.²⁰²

In Poland and Romania, budgetary payments for foreign trade enterprises were of dual nature: they resulted from a direct allocation of trade through plan targets under given prices. They also influenced the level of exports on certain products within the framework of multi-commodity targets - somewhat resembling a subsidy in the GATT sense.²⁰³ If subsidies were applied in the Hungarian system of trade control for exports to the market economies.²⁰⁴ However, at

the time of Hungary's accession to the GATT, they were being paid on a sector basis rather than on a product basis and were made public by the Hungarian authorities.²⁰⁵ This eliminated somewhat problematic issue of countervailable subsidies. In Hungary, subsidies were considered as temporary measures adopted to safeguard the balance of payments after the introduction of "new economic mechanism" and to permit some enterprises to shift progressively from their unprofitable product-mix to more profitable production.²⁰⁶ The purpose of subsidization was to eliminate the difference between the domestic and foreign prices when compared at the commercial exchange rate.²⁰⁷

As far as China's production and export system is concerned, subsidies are an essential instrument or means to develop its economy and expand its exports in the world market owing to its low-income economy.²⁰⁸ Production subsidies are granted to "infant industry" or export industries.²⁰⁹ Export subsidies are to increase the capacity of exporting products.²¹⁰ This is backed by a current policy to promote export and earn foreign hard currency.²¹¹ Since GATT has special arrangements for developing countries' export subsidies on primary products, and China is considered a low-income developing country and its export subsidization is mainly limited to primary products, thus China will be able to carry out the relevant GATT provisions.

3.5 CONCLUSIONS

Fundamentally, the GATT is based on market-economy view of world trade where state authorities which collect duties, fix standards and so on, are clearly distinct from the traders themselves. The GATT in its Article 17 recognizes state trading as a permissible form of trading although it was originally concerned only with occasional state trading as practised in the essentially private-enterprise system. The GATT approach to state trading is certainly acceptable for the loose state trading system where the character of the state trading link is limited either to state ownership of a trading enterprise or the granting of privileges which may give the trader a monopolistic position on the domestic market. Among state-trading systems in Hungary, Poland, Romania, China and the Soviet Union, the Hungarian and Chinese systems could be classified as loose state trading systems while the Polish, Romanian and the Soviet state trading regimes have the characteristics of the command systems.

Difficulties in the application of the GATT rules could arise in the case of command state trading systems, where it is possible to implement protectionist and discriminatory policies through the state trading link (basically plan targets) without recourse to the trade control instruments which are subject to GATT regulations. This leads one to conclude that if the command state trading systems are to be admitted to the GATT, new rules would have to be added to the

GATT code of conduct. Otherwise command state trading economies have to be decentralized to the extent to be compatible with the GATT requirements.

FOOTNOTES

- 1 GATT, Article 17:1(a).
- 2 GATT Article 17:1(b).
- 3 GATT *Basic Instruments and supplementary Documents* (hereinafter "BISD"), 9th Supp. 1961, p. 183.
- 4 This idea underlies provisions of Article 17(4)(b) of GATT. For a detailed discussion see Kostecki, *East-West Trade and the GATT System* (1979), p. 45.
- 5 GATT Art. 17 (1)(a).
- 6 Bernier, "State Trading and the GATT" in *STATE TRADING IN INTERNATIONAL MARKETS* (Kostecki ed. 1982), at 248; see also GATT Article 17 (3).
- 7 GATT, Art. 2(4).
- 8 Kenneth W. Dam, *The GATT: Law and International Economic Organization* (Chicago, London: The University of Chicago Press, 1970), p. 323
- 9 GATT, Interpretive note, Ad Article 2, para.4.
- 10 Note that Article 17, para. 3 only states that negotiations designed to limit or reduce obstacles to trade created by the operation of STEs "are of importance to the expansion of international trade". *Ibid.*, Art. 17:3.
- 11 Dam, *supra* note 8, at 324.
- 12 GATT Article 17: (1).
- 13 For a more detailed discussion of the concept of STEs, see Jackson, *World Trade and the Law of the GATT* (N.Y.: Bobbs-Merrill, 1969), pp. 339-45.

- 14 Bernier, *supra* note 6, pp. 245-260; Kostecki, *supra* note 4, p. 44; Lloyd, "State Trading and International Trade Theory", in *State Trading in International Markets* (Kostecki, ed. 1982), pp. 120-29; Harriet Matejka, "Trade Policy Instruments, State Trading and First-Best Intervention", pp. 142-160, in *State Trading in International Markets* (Kostecki ed. 1982).
- 15 See GATT Article 17:(1) which refers STEs to three types of enterprises: (1) state enterprises; (2) enterprises that have been granted a "special privilege"; and (3) enterprises that have been granted an exclusive privilege". See also Frieder Roessler, "State Trading and Trade Liberalization" in *State Trading in International Markets* (Kostecki ed. 1982), pp. 262-67.
- 16 Kostecki, *supra* note 4, p. 9.
- 17 With respect to the malicious characters of state trading, see Kostecki, *ibid.*, pp. 43-46, 65-70.
- 18 See Lloyd, *supra* note 14, pp. 118-20.
- 19 Those rules are: (a) maximize aggregate profits; (b) fix a profit margin per unit of sales; (c) zero profits; (d) a fixed price; (e) maximize gains from trade. (see Lloyd, *ibid*, p. 121).
- 20 *Ibid*, pp. 121-31.
- 21 *Ibid*, 131. the second proposition of Lloyd is: "for a given market segmentation, the instrument of a discriminating state trader and a set of ad valorem taxes-subsidies levied on competitive private trading are equivalent."
- 22 *Ibid*, pp 132-34.
- 23 *Ibid.*, p. 134. Nonetheless, they may remain "quasi-equivalent". States still have a choice between those instruments to achieve a single objective, though the choice is not a combination of the two but either state trading or tariffs or other measures.
- 24 GATT, Interpretive note to Articles 11, 12, 13, 14 and 18.
- 25 In NMEs, the volume of the imports is usually determined not by the margin between import prices and internal prices, but rather than by the plan. Dam, *supra* note 8, p. 326.
- 26 Dam, *supra* note 8, at pp. 326-27.

- 27 Suggested Charter for the ITO of the United Nations, Dept. of State Pub. 2598, in Commercial Series 93 (1946).
- 28 See Dam, *supra* note 8, p. 316.
- 29 *Ibid.* p. 317.
- 30 Bernier, *supra* note 6, at 250.
- 31 Dam, *supra* note 8, pp. 317-8.
- 32 The nondiscrimination in Art. 17 should be understood along with the "commercial criteria" essential in purchases or sales applicable to NME system. As para. 1(b) requires, "purchases and sales involving either imports or exports" are to be made "solely in accordance with commercial considerations, including price, quality, availability, marketability, transportation and other conditions of purchase or sale and shall afford other contracting parties adequate opportunity in accordance with customary business practice, to compete for participation in such purchases or sales." See GATT, Article 17(1)(b).
- 33 GATT Annex I, Ad Article 17 uses negative method to define "exclusive or special privileges". "Governmental measures imposed to ensure standards of quality and efficiency in the operation of external trade, or privileges granted for the exploitation of national natural resources but which do not empower the government to exercise control over the trading activities of the enterprise in question, do not constitute 'exclusive or special privileges". (Para. 1(a) of Ad Article 17).
- 34 Lloyd, *supra* note 14, p. 129.
- 35 *Id.* p. 129.
- 36 *Id.*
- 37 Kostecki, *supra* note 4, pp. 46-47.
- 38 *Id.*
- 39 *Id.*

- 40 See variety of articles and comments on the reform in PRC, namely, Falkenheim, "China Trade Reforms: Domestic Determinants and International Implications", in *EMERGING PACIFIC COMMUNITY* 131, 136 (R. Downen and B. Dickson eds. 1984); Friedman, "Enterprise Reform: The Three Li's", *CHINA BUSINESS REV.*, Mar. - Apr. 1985, at 24, 26; Prybyla, "The Chinese Economy", 25 *Asian Surv.* 538, 558 (1985); Xu Yi, "The Planned Economy and the Economic System", *CAIZHENG YAN JIU*, Jan. 31, 1984 at 21. translated in JPRS-CEA Doc. No. 84,038, MAY, 1984, at 50. (However the reform on-going, China must restrict economic spontaneity and maintain a planned economy to ensure that its economic activities conforms to the "objective law of socialist economy", 25 *ASIAN SURV.*, 998 (1985).
- 41 See GATT Doc. L/6270 (Nov. 27, 1987) the Working Party on China's Status as a Contracting Party - Questions and Replies Concerning the Memorandum on China's Foreign Trade Regime (hereinafter "QUESTIONS & REPLIES"), p. 84.
- 42 *QUESTIONS & REPLIES*, *id.* "A mandatory plan is an order with a legal compulsory nature imposed by the State and must be fulfilled," and an amendment or adjustment must be subject to the approval by the competent departments which made such plans; whereas "a guidance plan has no binding force, and its function largely depends on economic levers," and the guiding principle for planning coordination is: appropriate administration at macro level, increasing vitality at micro level and full use of the market mechanisms of supply and demand.
- 43 *Id.*
- 44 *Id.*
- 45 *Id.*
- 46 Regarding the main responsibilities of MOFERT, see *QUESTIONS & REPLIES*, *id.* p. 81.
- 47 *Id.* p. 81.
- 48 GATT, Doc. materials submitted to the GATT working party (unpublished).
- 49 K. Kennedy, "The Accession of the Soviet Union to GATT" (1987) 21 *J.W.T.L.* 23, at 33-35; Note, "Soviet 'Particip[ation]' in GATT: A Case for Accession", 20 *N.Y.U.J. Int'l L. & Pol.* 477, (Winter 1987), at 479.
- 50 Kennedy, *ibid.*, pp.34-35.
- 51 *Id.*

- 52 *Ibid.*, p. 35. Bialer & Afferica, "The Genesis of Gorbachev's World", 64 FOREIGN AFFAIRS 604 (1986).
- 53 *Ibid.* p. 49.
- 54 *Ibid.* p. 50.
- 55 *Ibid.* p. 51.
- 56 *Id.*
- 57 Bernier, *supra* note 6, p. 245.
- 58 Dam, *supra* note 8, p. 321.
- 59 *Ibid.*, at 245, 257.
- 60 Bernier, *supra* note 6, p. 246; See also GATT Art. 17 along with Art. 2(4) and an interpretive note to Articles 11-14, 18.
- 61 Bernier, *supra* note 6, p. 275.
- 62 See Lloyd, *supra* note 14, pp. 134-37. ("Invisibility" and "flexibility" are not advantages from an economic perspective; they instead increase the possibilities of harmful interventions as well as those of beneficial interventions. The outcome of the choices of invisible flexible state control will depend on the wisdom of these choices. It should be born in mind that the aim of GATT rules is provide common visible behavior so as to increase the stability and trasparency of the world trading system).
- 63 *Id.*
- 64 *Id.*
- 65 *Id.*
- 66 Roessler, *supra* note 15, p. 276.
- 67 Kostecki, *supra* note 4, p. 136.
- 68 *Id.* p.257.
- 69 *Id.*
- 70 *Id.*
- 71 Roessler, *supra* note 15, p. 274. According to GATT provisions, he classifies STEs into three types: (i) state-owned enterprises; (ii) privileged enterprises; (iii) government monopolies. *Ibid.*

- 72 *Id.* p. 274.
- 73 *Id.*
- 74 GATT, Interpretive note to Articles 11-14, and 18; Roessler, *supra* note 15, where he made a distinction between **RULES**, which are abstract and of general applicability, and **MEASURES**, which are applied in concrete circumstances to achieve predetermined results. *Ibid.*, at 261, 263, 275.
- 75 *Ibid.* at 275.
- 76 *c.f.* Kostecki, *supra* note 4, p. 51.
- 77 GATT, Art. 13:2(b).
- 78 GATT, *id.* There are five exceptions enumerated in the GATT which include:
- (a) quantitative restrictions are permitted to restore or maintain balance-of-payments equilibrium as provided by Article XII and in the case of the low-income economies by Article XVIII:B; (b) the low-income economies are also allowed to use quotas to assist the establishment of particular industries (Article XVII:C); (c) quantitative restrictions have continually used by the developed nations to protect agriculture; (d) quotas are also permitted to prevent market disruption (Article XXI; and (e) moreover, it is possible to use quantitative restriction against 'scarcity currency' countries (Article XIV). (See Kostecki, *supra* note 4, p. 52).
- 79 GATT, Art. 13. (QRs should be administered "on a nondiscriminatory basis.")
- 80 GATT Art 13:2(a).
- 81 GATT Art. 13:2(c).
- 82 GATT, Art. 13:1.
- 83 GATT, interpretive note, Ad Articles 11-14, and 18.
- 84 Kostecki, *supra* note 4, at 53.
- 85 GATT, Art. 12:4(d).
- 86 GATT, interpretive note, Ad Art. 12 4(e).

- 87 GATT Article 13:2(c); Kostecki, *supra* note 4, at 54. (Global licence permits conclusion of the transaction specified in the licence with any country, meaning it is not country-specific. The individual licence refers to a concrete transaction defining the import and export value of a given product with a given country and under established conditions).
- 88 GATT, Art. 13:2(c).
- 89 GATT, Art. 13:2(c).
- 90 GATT, Art. 13:3(a), 3(c).
- 91 GATT, interpretive note to Articles 11-14 and 18.
- 92 Note that nondiscriminatory operation of state trading enterprises has been incorporated into Art. 17 of GATT.
- 93 However, para. 4(c) of GATT Art. 17, does require CPs maintaining STEs, upon request of being adversely affected party, to supply information about their operations of state trading. See GATT, Art. 17:4(c).
- 94 Kostecki, *supra* note 4, p. 54.
- 95 *c.f. supra* note 87.
- 96 GATT Doc L/3301, Jan. 1970, pp. 19-21 and 29.
- 97 Kostecki, *supra* note 4, p. 73.
- 98 *Id.*
- 99 *Id.*
- 100 *QUESTIONS & REPLIES, supra* note 41, p. 118.
- 101 *QUESTIONS & REPLIES, id.*
- 102 *QUESTIONS & REPLIES, id.*
- 103 *QUESTIONS & REPLIES, id.*, pp. 120-21.
- 104 *QUESTIONS & REPLIES, id.* p. 121.
- 105 *QUESTIONS & REPLIES, id.* p. 125.
- 106 GATT, Art. 11.
- 107 Castel, *International Business Transactions* (Carswell, 1988), at 41.
- 108 Para. 1 of GATT Article 11 states that,

"No prohibition or restrictions other than duties, taxes or other charges, whether made effective through quotas, import or export licences or other measures, shall be instituted or maintained by any contracting party on the importation of any product of the territory of any other contracting party or on the exportation or sale for export of any product destined for the territory of any other contracting party." Ibid., GATT Art. 11:1.

- 109 Kostecki, *supra* note 4, at 55.
- 110 A formula for exchange of concessions of same nature. For instance, tariff reduction is exchanged for tariff reduction. See Kostecki, *supra* note 4, at 40.
- 111 Kostecki, *supra* note 4, p. 41.
- 112 *Id.*
- 113 *Id.* (A formula providing exchange of concessions of different nature such as exchange tariff reductions with import increase undertakings).
- 114 *Id.*, at 41, 55.
- 115 *Id.* p. 58.
- 116 *Id.* at 73, 74. Note that the situation has changed lately.
- 117 *Id.* at 74.
- 118 GATT Doc. L/6125, (18 Feb. 1987), "China's Status As a Contracting Party: Memorandum on China's Foreign Trade Regime," (hereinafter MEMO), at 13.
- 119 See Regulations on Import and Export Duties of PRC of 1984.
- 120 *QUESTIONS & REPLIES*, *supra* note 41, pp. 87-88.
- 121 *QUESTIONS & REPLIES*, *supra* note 41, at 89.
- 122 *Ibid*, p. 101. "Substantial transformation" means that the manufacturing or processing operations of the products entail a change in the 4-digit tariff heading of the Customs Import and Export Tariff, or the percentage of the value added is over 30% of the whole value of new product. (See Regulations on Import and Export Duties of PRC 1984.)
- 123 *QUESTIONS & REPLIES*, *supra* note 41, p. 103.

- 124 *QUESTIONS & REPLIES*, *supra* note 41, at 102, 103.
- 125 GATT Art. 6 and the Antidumping Code (1979) GATT Doc. MTN/NTM/W 236. For analysis see Jackson, *supra* note 3, pp. 411-24. "Dumping" is a form of international price discrimination whereby a producer charges a lower price for its product in a foreign market than it charges for the product in its domestic market. Dumping occurs when the product is sold in a foreign market at a price that is less than the product's fair value. See J. Viner, *Dumping: A Problem in International Trade* (1923 & reprint 1966).
- 126 Kostecki, *supra* note 4, p. 58.
- 127 GATT, Art. 3:9.
- 128 GATT, Art. 3:4.
- 129 GATT, Art. 2:1(c).
- 130 GATT, Art. 2(4).
- 131 J.H. Jackson, *Legal Problems of International Economic Relations* (1986 2d ed), p. 1179; Kostecki, *supra* note 4, p. 57; Dam, *supra* note 8, p. 318.
- 132 Jackson, *id.*, p. 1179; Kostecki, *supra* note 4, p. 58.
- 133 Kostecki, *supra* note 4, pp. 79-80.
- 134 *Id.* p. 79.
- 135 A system of price equalization (equalization system) was maintained in Poland and Romania to turn the importer's profit over to the state and to offset the exporter's loss out of the state budget. The reason for adopting this system was because it can compensate differences between the export revenues and import expenses converter at the official exchange rate which was not an equilibrium exchange rate. *Id.*, p.79.
- 136 *Id.* pp. 79-80.
- 137 *Id.* p. 80.
- 138 Kostecki, "Hungary and GATT" 8 *J.W.T.L.* 401, at 406.
- 139 Kostecki, *supra* note 4, at 79.
- 140 Kostecki, *supra* note 4, p. 81; also *supra* note 138, pp. 411-12.
- 141 Kostecki, *supra* note 138, pp. 407-8.

- 142 MEMO, *supra* note 118, at 6.
- 143 QUESTIONS & REPLIES, *supra* note 41, pp. 135-36.
- 144 MEMO, *supra* note 118, at 19.
- 145 MEMO, *id.*
- 146 MEMO, *id.*
- 147 MEMO, *id.*
- 148 K. Kennedy, *supra* note 49, p. 27.
- 149 *Id.*
- 150 *Id.*
- 151 See Berman, Banstin, "The Soviet System of Foreign Trade", in BUSINESS TRANSACTIONS WITH USSR, (R. Starr. ed. 1973).
- 152 See GATT Doc. MTN/NTM/W 236, *supra* note 125.
- 153 In determining whether or not there are material injuries, an appropriate understanding of the concepts of "domestic industry" and "like product" is most crucial. See Langer, "The Concepts of Like Product and Domestic Industry Under the United States Trade Agreements Act of 1979", (1983) 17 *Geo. Wash. J. Int'l L. & Econ.* 495; Palmeter, "Injury Determinations in Antidumping and Countervailing Duty Cases--A Commentary on U.S. Practice", (1987) 21 *J.W.T.L.* 7.
- 154 GATT Article 6:2, 3.
- 155 GATT Article 6:6. Material injury test is the thrust of GATT antidumping and Subsidies Codes. See, Palmeter, *supra* note 153.
- 156 Palmeter, *id.* at 19.
- 157 GATT Article 6.
- 158 GATT Article 6:2, 4.
- 159 R. Paterson, *Canadian Regulation of International Trade and Investment* (Carswell 1988), at 140. (discussing functions of Track I-Articles 7-13 of Subsidies Code and Track II-Articles 1-6 of the Code).
- 160 GATT Article 16:4.
- 161 GATT Article 16:3.

- 162 GATT Article 16:1.
- 163 GATT Article 16:1.
- 164 GATT Article 16:3.
- 165 GATT Article:4.
- 166 GATT Article 6.
- 167 GATT, BISD, 9th Supp. 1961, at 191.213
- 168 For explanation, see Kostecki, *supra* note 4, at 55, 77-78. ("the equalization system as practised in Poland and Romania could not be considered subsidizing in the GATT sense.") *Id.*, at 78.
- 169 *Id.* p. 57. For definition of equalization system, see note *supra* 135.
- 170 However, it is up to each member of GATT to determine whether countervailable. GATT BISD, supp. 1961, p. 191.
- 171 See generally Samuelson, *Economics* 620-30. (11th ed. 1980) (explaining the theory of comparative advantage). Comments, "Implementation and Policy: Problems in the Application of Countervailing Duty Laws to Nonmarket Economy Countries" 136 *University of Pennsylvania Law Review* 1647, (1988).
- 172 T.R. Howell & Alan Wm Wolf, "The Role of Trade Law in the Making of Trade Policy" in *International Trade Policy: The Lawyers' Perspective* (J.H. Jackson, R.O. Cunningham and Claude G.B. Fonthem ed. 1985), at 3-11, 3-15-19. (discussing primacy of the rule of law on competition and current U.S. trade remedies for domestic industries suffering material injury resulting from unfair trade practices).
- 173 H.M. Applebaum, P.G. Gaston, "What is a 'Domestic Industry' for Purposes of Application of the U.S. Trade Laws" in *International Trade Policy: The Lawyers' Perspective* (J.H. Jackson, R.O. Cunningham and Claude G.B. Fonthem ed. 1985), at 13-11-17.
- 174 S.M. Rosen & C.H. Bayar, "Comparing Causes of Injury Under the Escape Clause" in *International Trade Policy: The Lawyers' Perspective* (J.H. Jackson, R.O. Cunningham and Claude G.B. Fonthem ed. 1985), at 5-1-23.

- 175 Jackson, *Implementing the Tokyo Round* (1984) (gives a comparative study of three trade partners' trade law after the Tokyo Round multinational trade negotiations). In Canada, rules against dumping/subsidy are incorporated into Special Import Measures Act of 1984 (SIMA); in the United States Trade Agreements Act of 1979; in Japan and EC, there have been incorporated into special law and procedures governing the imposition of antidumping and CVD duty. But Japan, due to its aggressive export policy, the antidumping law is basically dismantled. In the alternative, it is compelled to enter into various so-called voluntary export restraints (VERs) with its leading trade partners.
- 176 Kostecki, *supra* note 4, p. 58.
- 177 *Id.*
- 178 Soltysinski, "Price Competition Between Free-Market and State-Controlled Economy Enterprises: The Legacy of the OMC v. Pezetel Litigations", 24 *Swiss Rev. Int'l Competition L.* 6. ("[T]he frequency and scope of state intervention in the market is incomparably wider in the centrally planned economy countries [than in market economies].").
- 179 P. Samuelson, *supra* note 171, at 39-41.
- 180 *Id.*
- 181 *Id.*, at 821-23.
- 182 *Id.*, p. 823.
- 183 *Id.*
- 184 Downey & Graham, "The Regulation of Dumping from State Controlled Economies: Where Next?" in *INTERFACE TWO: CONFERENCE PROCEEDINGS ON THE LEGAL FRAMEWORK OF EAST-WEST TRADE* 435, at 438-439. (D. Wallace & D. Flores eds. 1982).
- 185 A surrogate approach is used to determine the normal value of NMEs' imports by having reference to the price of the like product to be sold in a third market economy country. For a detailed explanation, see Jackson, *supra* note 131, pp. 697-99. Article 15(2) of Subsidies Code provides that:

It is understood that in [the case of nonmarket economy] countries the calculation of the margin of dumping or of the amount of the estimated subsidy can be made by comparison of the export price with: (a) the price at which a like product of a country other than the importing signatory...is sold, or (b) the constructed value of a like product in a country other than the importing signatory...".

The Agreement on Interpretation and Application of Articles 6, 16 and 23 of the GATT (Subsidies Code), April 12, 1979, 31 U.S.T. 513. T.I.A.S. No. 9619; GATT BISD, 26th Supp. 56 (1980), at 74.

186 Comment, *supra* note 171, at 1669-70.

187 *Id.* p. 1667.

188 *Id.* p. 1669.

189 See Textiles, Apparel, and Related Products from PRC, Dept. of Comm. Docket No. C570-005; 48 Fed. Reg. 46,400 (Dep't Comm. 1983) (initiation) (hereinafter CVD Petition). See Recent Development, "Countervailing Duties and Non-market Economies: The Case of the People's Republic of China," 10 *Syracuse J. Int'l L. & Competition* 405, pp. 418-20 (1983) (rejecting the application of CVD laws against NME as an ethnocentric value judgment).

190 *Carbon Steel from Poland*, 49 Fed. Reg. 19,374 (Dep't Comm. 1984) (final det.); *Carbon Steel from Czechoslovakia*, 49 Fed. Reg. 19,370 (Dep't Comm., final det. 1984).

191 *Carbon Steel from Czech.* *id.*, at 19,371.

192 Recent Development, "International Trade: Imposition of Countervailing Duty Laws on Products From Nonmarket Countries--Continental Steel Corp. v. United States", 27 *Harv. Int'l L. J.* 745, 749 (1986).

193 801 F. 2d 1308, (Fed Cir. 1986).

194 *Id.*, 1315-16.

195 *Id.*

196 Comment, *supra* note 171, at 1665.

197 *Id.*, pp. 1665-67; see Trade and Int'l economic Policy Reform Act of 1987, H.R. 3, s. 157, 100th Cong. 1st Sess. (1987) (applying the CVD laws to NMEs to the extent that a subsidy can be identified and quantified by the administering authority (hereinafter 1987 Trade Bill)).

- 198 Comment, *supra* note 171, at 1652, 1671; See also Denton, The Nonmarket Economy: Rules of the European Economic Community's Antidumping and Countervailing Duties Legislation," 36 *Int'l & Comp. L.Q.* 198, 236 (1987) ("[I]n [nonmarket economies] it can be argued that dumping and subsidies are but two sides of the same coin").
- 199 See, e.g., Rawson, "An Outline of United States Regulation of Trade with Non-market Economy Countries," in *INTERRACE TWO*, *supra* note 184, at 538. (noting that use of surrogate country procedures in an antidumping case would, in effect, "transferring a countervailing duty case into an antidumping case"); Comment, "Georgetown Steel corp. v. United States: Applying the Countervailing Duty Law to Imports from Nonmarket Economy Countries," 18 *Law & Pol'y Int'l Bus.* 313, at 332 ("adoption of the surrogate method would mean that antidumping duty and CVD petitions involving imports from NMEs would be almost identical."); Note, "An Argument for Freer Trade: The Nonmarket Economy Problem under the U.S. Countervailing Duty Laws," 17 *N.Y.U.J. Int'l L. & Pol.* 407, 425 (1985). ("subsidization and dumping are similar conception in the nonmarket setting because there is no private sector of the economy.") Despite the above comments, one should note the latest dramatic changes in East Bloc.
- 200 Comment, *supra* note 171, pp. 1671-74.
- 201 Kostecki, *supra* note 4, pp. 78-79.
- 202 *Id.* pp. 78-79.
- 203 *Id.* p. 79.
- 204 Kostecki, *supra* note 138, at 409.
- 205 *Id.*, pp. 409-10. (However, the Hungarian export subsidies could be considered as compatible with the GATT as long as Hungary fulfilled the obligations of GATT imposed on all the contracting parties maintaining subsidies). Note that there are two obligations imposed on CPs: (a) not to grant export subsidies on primary products that would result in "more than an equitable share of world export trade." (Art. 16:3); (b) to notify GATT about any export subsidy if used. (Art. 16:1).
- 206 Kostecki, *supra* note 4, p. 78.
- 207 *Id.* p. 78; see also *Economic Survey of Europe* (N.Y.: United Nations, 1969), p. 102.
- 208 MEMO, *supra* note 118, pp. 10-11.

209 MEMO, id., p. 10.

210 MEMO, id.

211 MEMO, id.

P A R T F O U R

RECONCILIATION OF NME WITH GATT FRAMEWORK

Although GATT reluctantly admitted some non-market economies into its framework, it did not solve the problem of non-discrimination and reciprocity problem. The dominant GATT approach to NME's accession was basically modelled on a country-to-country basis with pragmatically import-commitment-oriented character. This approach has been unsuccessful contributing to the growth of East-West trade relationship. A re-evaluation of the strengths and weakness of the approach is necessary. Efforts would be made to suggest workable options for improvement. The options will be discussed in the context of China's accession to GATT, and directed to the problem of reconciliation and reintegration of world trade systems. The focus of the following discussion will be on analyzing various possibilities to ascertain which option would be best for reconciling the NME with the GATT trade rules.

4.1 WEAKNESS OF GATT APPROACHES TO STATE TRADING SYSTEM

In defining state trading enterprises Art. 17 equivocates an important distinction between private enterprises that benefit from subsidies granted openly in market economies as part of the political process (so-called "privileged

enterprises") and publicly-owned enterprises that are assisted as part of the operation of the enterprise (state-controlled enterprises").¹ It is important to clarify their distinction because as a normal practice, when a government gives a subsidy to a private firm, its actions are transparent and the problems of detection and quantification of the subsidy are not as complicated as when the subsidies are provided completely internally.² It is submitted that an appropriate definition of STEs should cover only those enterprises that are substantially government-owned or controlled. Accordingly, the privileged enterprises should be excluded from the category of STEs. This would render the definition politically neutral and would base it on an objective determination rather than on the motivation for or the effects of the enterprise's activity.³ It is also submitted that the GATT definition of STEs should encompass not only state-owned or controlled enterprises but also state agencies granting special or exclusive privileges.⁴

As noted earlier, it would appear illogical or illusory to request STEs especially those established in NME countries to be operated "solely" according to the commercial standard. It is better to delete the original wording "solely" in para. 1(b) since considerations cannot be, in reality, "solely" commercial but rather a mixture of social, political and commercial factors.⁵ Para. 1(b) should therefore be modified to provide a more realistic standard for the operations of STEs.⁶

In addition, it is important to note that the GATT's emphasis on regulating STEs' behavior on enterprises is misplaced because it is government not enterprises who is in a position to grant special or exclusive privileges.⁷ This is particularly true in some NMEs where enterprises are merely to accept governments' plan and directions. Secondly, in today's mixed economies, the distinction between private and state-controlled enterprises has been blurred simply because governments in the developed world have acquired tremendous discretion to subject all enterprises to specific measures.⁸ Therefore, the focus of the GATT on trade liberalization should be on individual countries' commercial policies and legislations.⁹

Applying such a concept of state trading would imply that not only import monopolies but also the operations of a government agency would be subject to the same rules and requirements articulated in the GATT provisions.¹⁰ As a result, the reporting requirement enunciated in Art. 17 would be applied not just to the above noted privileged enterprises but also to government agencies granting special privileges or giving operative directions.¹¹ In this respect, it would be more meaningful for the GATT to make distinctions between "forms" of government intervention (rules/measures) rather than distinctions between "objects" of governments intervention (private/ State-controlled enterprises).¹²

4.2 A PRELIMINARY EVALUATION OF THE IMPORT COMMITMENT APPROACH

As indicated earlier, GATT was drafted mainly for market economies controlling their trade essentially by means of pricing mechanisms and resorting to state trading only on an occasional basis. Difficulty could therefore be well expected in applying its provisions to state trading economies whose trade is controlled by means of targets, especially with regard to the GATT principles of non-discrimination and reciprocity and to the GATT rules on integration.¹³

The basic problem to be solved at the time of Eastern bloc's accession to the GATT was the problem of market access. This was solved by way of finding reciprocity formula varying from country to country. And the problem of finding a reciprocity formula for trade with the target-protected economies are usually approached by a commitment either to increase import or to reduce level of protection.¹⁴

Article 17 of GATT directs STEs to be operated in a fashion in compliance with non-discrimination and commercial considerations. But when dealing with NMEs' accession to GATT, GATT countries employed the standard of "fair import expansion" rather than non-discrimination.¹⁵ After the fair import expansion method had been used, the GATT countries expressed satisfaction with the geographical development of Hungarian, Polish and Romanian imports.¹⁶ This is because such approach is more realistic and pragmatic. One would wonder what better approach would have been undertaken in the absence

of this approach. However, some better approaches do exist namely the revision of GATT Article 17, incorporation of new provisions into the GATT and requiring full decentralization of NME state trading systems so as to be compatible with the GATT framework. But these approaches are too unrealistic and time-consuming to worth pursuing. It is unrealistic because some of NMEs are not prepared to utterly accept the market principles for the time being. And the market economies of GATT members are not willing to change their well-established market notion. Furthermore, it is not likely that the GATT rules will be fundamentally changed. It is time-consuming because even if NME nations such as China and the USSR were to change their systems into market type, it would take a considerable amount of time to complete. Their full decentralization cannot be expected to be accomplished within five or even ten years. Moreover, it is reasonable to assume that even if some of the better approaches were being taken, the Eastern bloc would not have acquired GATT membership.

This is certainly not to discourage the continuing pursuit of better approaches. It is perhaps the right time, at least intellectually, to reconsider the fundamental ideologies of the GATT economic and legal system especially as more and more weaknesses of GATT have been exposed. Some of GATT's weaknesses originated from its inception. Some of its assumptions may be out of date as time elapses. As far as the fair import expansion approach is concerned, it is questionable as to whether the accession of Hungary, Poland

and Romania to the GATT has brought a more multilateral character to these countries' trade with GATT members.¹⁷

As to reciprocity between East and West, the above-mentioned arrangements have proved disadvantageous to the three East European countries at least from the perspective of balance-of-trade between East and West.¹⁸

Taking the Polish accession to GATT for an example, apart from little concern with the balance-of-trade criterion of reciprocity, the import commitment approach to Poland's accession discourages Poland to increase import beyond the target amount.¹⁹ Such formula is contrary to GATT philosophy and the interests of most CPs because it supports the administrative measures and state control that are possible to guarantee fixed import levels while discouraging decentralization and other economic reforms that increase the role of market forces.²⁰ The obligations imposed on such formula can be discharged by various means available to NME government.²¹ Since the volume of imports into NMEs is to be evaluated on the basis of current dollar prices, its value and burden can be eroded by inflation and increased by deflation.²² More than that, because the commitment is denominated in a particular currency its value can be affected by manipulation of the exchange rate by the state.²³ Furthermore, the import commitment formula seems indifferent to special arrangements between CMEA countries, it leaves open the door of discrimination between imports from the West CPs and those from CMEA countries. Finally, it does not seem to be

an appropriate framework in determining Western market openings for Polish exports.²⁴

The Romanian import commitment negotiated several years later overcame some of Poland's weaknesses as it undertook to develop and diversify its trade with the CPs as a whole. It stated its "firm intention" to increase imports from the cps as a whole at a rate not smaller than the growth of total Romanian imports provided for in its five-year plans.²⁵ Some might have interpreted this formula as non-discriminatory. Unfortunately the fulfillment of the commitment does not guarantee non-discrimination.²⁶ It is possible that over time imports from CPs would increase at a faster rate than those from the Eastern bloc.²⁷

Worse than that, the formula is hardly enforceable due to the ambiguity of "develop and diversify" and "firmly intend."²⁸ The commitment is based on provisions in the plan rather than actual import levels. It is therefore subject to manipulation.²⁹ However, this "unenforceability" should not be overstated since any international agreement more or less has certain level of "flexibility" and "ambiguity" available for governmental manipulation and abuse.³⁰ GATT is notorious in this regard. Ironically, it is perhaps this flexibility and vagueness that makes the import expansion formula easily acceptable and more workable than the rigid obligation imposed on Poland's accession to GATT.³¹

Stressing the demonstrated shortcomings of import commitment approach and increasing role of market forces in

its economy, Hungary acceded to the GATT on the basis of tariff concessions without any import commitment.³² However, during the working party session on its protocol, Hungary did undertake to increase its imports from the cps-though not as firmly as Poland and Romania did.³³ Here again, market access issue remained unsolved.

The problems with use of the import commitment would be more evident in the context of China's accession. Here the weakness of the precedent is more revealing than ever. Not surprisingly, the GATT members will be tired of any Chinese import commitments when unstable and non-transparent trade policies are still in sight.³⁴ Even if that is not the case, it remains unrealistic to expect a specific import commitment when the on-going economic and foreign trade reforms are according entities and enterprises much more power in trading with foreign partners.³⁵ This is particularly true when trade volumes are not entirely determined or controlled by the government.³⁶ As China's trade policies become more flexible, an import commitment with a rigid nature will obviously limit China's discretion in dealing with world trade.³⁷ Although a "modified import commitment scheme"³⁸ containing a set of detailed specific provisions might be able to introduce a sense of flexibility, the fundamental problems with import commitments are "the weak precedent for use, their incompatibility with the reforms now under way, the rigidities and market foreclosure they leave in place".³⁹ This would probably remain unsolved.

Admittedly, the GATT fair share of import expansion approach failed to provide an effective framework for non-discrimination in East-West trade. It did not reduce the Western counterpart's discriminatory quantitative restrictions on Eastern European exports. It did not successfully solve the problem of non-discriminatory operations of foreign plan targets in Poland and Romania. Instead of settling the matter on the basis of nondiscrimination, the GATT preferred a pragmatic and rather implicit solution based on a requirement of 'fair' import expansion. This fair share is scrutinized according to the geographical development of their imports during periodic consultations. Unfortunately it did not touch the basis of non-discrimination for the reasons that Poland, Romania and Czech being GATT members were unable to effectively use the instrument for concession-making and import increases (market openings) as a bargaining element to attain reciprocal market openings in the West. Secondly, the so-called "import-commitment approach" is too politically-minded to have necessary economic meaning.⁴⁰

Equally unfortunate, the approach spells almost nothing about protection and non-discrimination⁴¹ both of which are the twin themes of the GATT.⁴²

The above weaknesses of the approach would be sufficient to force one to rethink the validity and effects of the approach with a view to improving it by exploring better alternatives to replace the existing arrangement. The task of reforming the GATT system towards integrating NME countries

would be attainable in the context of the following two options:

(1) Improving the existing technical arrangements while maintaining its present stand on the country-by-country approach;⁴³ or

(2) Discovering new approaches to adapt the GATT to the changed economic and political realities of East-West cooperation.⁴⁴

4.3 IMPROVING THE EXISTING ARRANGEMENTS

As the theme of negotiations on the terms of NMEs' accession centers around "reciprocity" (market openings) and "entrance fees", improvements could be guided by such the assumption that:

"If NMEs are to be integrated into the main stream of the GATT an entrance fee must be devised which is both workable and considered by both sides to represent equitable compensation for the benefits received by the acceding NME."⁴⁵

Based on this assumption the entrance fee or terms of accession should be the one with which NME's compliance can be easily monitored.⁴⁶ This would require sufficient transparency in respect of the functioning of NME's political-economic systems for the purpose of determining market openings for GATT cps. This could be achieved by a modified and refined import commitment which requires that a firm obligation and not a mere promise be undertaken. It also requires a direct link between import and export levels, the assurance of

national treatment (non-discrimination between imports and domestic production), and the evaluation of reciprocity on the basis of balance-of-trade criteria. Finally, it requires the readjustment of import target to reflect changes in price levels.⁴⁷

It is note worthy that even though these proposals were able to improve the existing arrangements made for Poland and Romania, they would be unable to function in the case of negotiations with China's accession as mentioned earlier.

Any improvement of the existing arrangements provided for East European accession should be aimed at two different aspects. Weight and attention should be given to improving the negotiations of concessions on the basis of targets.⁴⁸ The new approach should consider the likelihood of wider participation of other NMEs such as China and Soviet Union in the GATT forum on the basis of tariff protection.⁴⁹

All approaches toward state trading may be classified into two broad categories: those which deal with commercial policy measures and those which deal with trade effects.⁵⁰ The acceptability of the former category rests on the assumption that state trading implies no further restraint on trade than the nominal commercial policy measures imposed on the products it covers.⁵¹ Verification of this assumption would require product-by-product investigations. This is impracticable since state trading has wide coverage.⁵² The "trade effects" approach, on the other hand, offers a means by which concessions may be defined simply and surveillance conducted

easily.⁵³ However, one would have to note that negotiations on trade targets are not necessarily easier than those on commercial policy measures.⁵⁴ Focus should be placed on ensuring that state trading practices are neither restrictive nor discriminatory.⁵⁵

4.4 DISCOVERING NEW APPROACHES TO RECONCILIATION

It should be borne in mind that the basic objective of the new approaches is to widen the possibility of eventual more extensive participation of the socialist countries in the GATT. Such new approaches should not limit the GATT's role in the ever more important sphere of East-West trade. With this aim in mind, the possibility of reconciliation can be considered.

Obviously to make a reconciliation of NME and the GATT is to make a reconciliation of NME and market economies. To this end, market economies, on the one hand, should consider NMEs' practical difficulties in completing their economic reforms or readjustments to join the GATT and their positive efforts in participating in today's world trade system. GATT should be more tolerant and cooperative towards NME participation. It is well proved that the success of GATT multilateralism is due to its flexibility to tolerate and compromise conflicting ideas and different national interests. Without such compromise, some consensus could have never been reached. Without such

flexibility, GATT cannot play any decisive role in world trade.

Certainly, non-market economies should expect less change in GATT rules or market economies' structure and readjust and reform their economic systems so as to be compatible with the established GATT legal system. With regard to this, the U.S. as a super power will probably take advantage of NME accession to use the GATT framework as a ball to require NME's full decentralization. However, U.S. will have to yield to the interests of EC and other middle-sized trading powers. EEC countries and most middle-sized traders have positive attitude towards NMEs' participation in GATT.

What has been said is to stress that the task of reconciling NMEs with GATT trade rules would occur in both directions as earlier discussed. One-sided concession is neither realistic nor fair. It is unrealistic because any of two sides who is only insisting in concessions of another party and who never makes his own concessions would simply spoil the possible reconciliation. This is particularly true when both are demanding concessions and concessions of one side are conditioned by that of the other. It is unfair because in today's world of mixed economy, virtually every country has a certain degree of monopolies. State control over trade becomes epidemic in both capitalist and socialist countries. What makes the difference is merely a matter of degree of control.⁵⁶

With a view to widening the possibility of reconciliation, GATT contracting parties especially those major market economies should first of all overcome the ideological difficulty in understanding the realistic possibility of political and economic peaceful co-existence between East and West. Once this is done comprehensive solutions can then be considered and further be worked out to resolve the task of integration.

The GATT can maintain the previously adopted "gradual and pragmatic" approach to accept countries like PRC into its membership despite the fact that their reforms are not yet finished and their economies are still in a transitional period of plan and market. Upon their accession to the GATT, the GATT Contracting Parties might take measures to request those members who, after accession, are still not in full conformity with GATT rules to make further adjustments and reforms. This is crucial in expanding the influence of the GATT as a broader world trade organization. In the case of necessity, the GATT ought to seek other remedies outside its original framework. And this was what the GATT actually undertook to solve the problem of market access to East European countries. In addition, the GATT should continue to approach the subject matter gradually and realistically.⁵⁷

4.4(1) GRADUAL AND REALISTIC APPROACH

This approach was first used by the GATT to deal with East European NME countries' accession to the GATT. It was justified by the fact that almost all NMEs, regardless of their willingness to accept the market principles illustrated by the GATT, cannot complete their economic and foreign trade regimes within a short period of time. When NMEs revealed their interest in participating in the GATT trading system, the option left for the GATT contracting parties were either to refuse their applications or accept them first and then negotiate with them until they are able to carry out the GATT requirements. Realizing that rejection is meaningless and fruitless, the GATT adopted the gradual and realistic attitude towards Eastern bloc's integration. This approach remains valid for dealing with China or the Soviet Union's accession to the GATT.

"Gradual and realistic" primarily means that the GATT can accept the NME into its membership on a step-by-step basis. For instance, in the case of China's accession to GATT, the GATT working party and China could establish criteria to serve as "milestones" or "graduation" method in determining whether China could accede fully to the GATT.⁵⁸ As indicated earlier, there is no absolute definition of "market and "non-market". The distinction between market and non-market is only relatively determined. During the stage of "milestone", China and GATT member nations should focus on the essentially

practical goals that underlie the GATT. These are maximizing the opportunity for economic exchange among the countries that want to trade with each other and maintaining a sense of fairness so that the system will enjoy continuing support in each country.⁵⁹ The milestones should be sufficient to justify that there is a large and free market in China opening to the GATT countries. The free market is achieved by freedom of pricing and transactions.⁶⁰ The ultimate compatibility of China's trade and tariff system with the GATT depends on whether or not China is able to achieve the following milestones:

(1) relaxation of price controls on major categories of products, with prices responding to supply and demand,

(2) reduction of price controls on the inputs used in making such products,

(3) gradual elimination of central planning measures so that purchasing decisions are made on the basis of price, quality and other commercial factors, rather than upon administrative quotas or goals,

(4) decentralization of economic decision making so there would be a plurality of Chinese enterprises competing with each other to purchase foreign products,

(5) substantial elimination of export subsidies and trade-distorting internal subsidies,

(6) availability of information concerning potential Chinese purchasers, their needs, and procedures for doing business with them,

(7) an adequate legal framework to ensure that foreign suppliers and purchasers can enter into valid contracts with full protections for proprietary information, patents, technology transfer and the like, and

(8) the presence of a codified and uniform tariff system.⁶¹

Among these milestones, China has met in part, (1), (2), (3), (4) and (6). As for the fifth requirements China can use some of the exemptions provided by the GATT for developing countries.⁶² As far as the seventh requirement is concerned, they will be gradually fulfilled. With respect to the tariff system, it is already codified and accessible.⁶³ However, China employs different tariffs for open cities and Special Economic Zones (SEZs). If tariffs system applicable to the SEZs and those open cities listed could be implemented in the entire trading system, it would certainly be easier for China to accede to GATT on a tariff reduction basis.⁶⁴

While using milestone method to test NMEs' compatibility with GATT, some specific provisions for "graduation" from observer status to full membership should be included in every area in which NMEs are initially subject to special treatment.⁶⁵ Polish and Romanian import commitments should be renegotiated as they now adopt a custom tariff to be an effective instrument of trade regulation.⁶⁶ In addition, the discriminatory QRs on NME products should be eliminated if the NMEs had adopted a transparent economic system to which the regular GATT provisions on market disruption can be applied

effectively.⁶⁷ As to whether special rules applied to low-priced imports from NME should be maintained or not, it should rely on whether market forces are operative in the domestic market of the NME countries.

To avoid unnecessary arguments and minimize disputes in determining the status of the NME's economy, a panel and working party should be established to use a set of commonly accepted criteria and guidelines for investigations and annual review.⁶⁸

A step-by-step and milestones examination can begin with the marginal status of observer in various GATT committees of special interest such as agriculture, textiles and/or in particular MTN codes.⁶⁹ And this could be followed by the observership in the GATT, provisional accession based on tariff negotiations (type of quasi-membership or "experimental association"⁷⁰ and finally full membership. During experimental association with the GATT, NMEs should conduct their commercial relations with other cps in accordance with the GATT "to the extent possible" under its economic system.⁷¹ This is the so-called "second class membership" which some NMEs such as China and the Soviet Union would be unhappy with. However, it can be used as a transitional phase and once the NME has passed this stage, it can acquire full membership. The periodic consultations coupled with the "milestones" examinations would certainly help the working party to evaluate the NME's economic development and its compatibility with the GATT multilateral framework. If compatible enough,

the special safeguard clauses imposed provisionally by cps could be removed and replaced with the normal safeguards available in Article 19.⁷² The length of time of observership and associate membership of NMEs needed for acquiring full membership would depend on the economy of individual NMEs and their willingness to accept "special terms" of accession.⁷³ Normally, as soon as the milestones have been achieved and reciprocity formula for solving market access problem agreed upon, full GATT membership would be granted with no more complications.⁷⁴

The advantage of using this approach is that both GATT cps and NMEs applicants have the opportunity to be conversant with each other during the transitional periods.⁷⁵ The NMEs may take advantage of the steps to be familiar with the GATT as a contract as well as an institution which has proved beneficial in negotiating their terms of membership as well as living under them.⁷⁶ On the other hand, GATT countries can be well informed of every development and progress made in the NMEs.⁷⁷

In any event, what remains to be determined is whether the traditional practice of dealing with each NME on an individual basis should be continued or whether it is preferable, now that a significant amount of world trade involves NMEs, to amend the GATT by adding general provisions addressed to the common problems involved in NME participation.⁷⁸ Some of the advocates suggest that further provisions should be added to the GATT as "Part V", the so-

called "Part V approach".⁷⁹ Regardless of the possible merits of this approach, Each NME has its own non-common characteristics. Some are command state trading systems. Others follow loose state trading system. Still others are relatively developed such as Yugoslavia and Hungary. There are also those that are low-income economies such as Romania and China. The question as to whether a NME is able to fulfill its obligations (*pacta sunt servenda*) is not determined by a simple label of NME attached to all NMEs in different stages of development following a bit different trading systems.⁸⁰ The merit of adopting individual protocols is that it deals with different NME on country-by-country basis. On the other hand, the merit of protocols is undermined by its disadvantages which can be overcome by an overall approach.

Thus a combination of individual approach and overall approach would be most preferable. The GATT CPs can, on the one hand, incorporate new provisions accommodating the NME along the lines as suggested in the unfulfilled "Havana Charter". This can be done by providing general rules applicable to all NMEs with common characteristics. As to whether they should be added to GATT as Part V deleting Article 17 or can be combined with a revised Article 17, it should depends on convenience. The GATT can have variation due to the fact that each individual NME has its own unique situation. For instance, China as an original contracting party would prefer to resume her membership instead of acceding to the GATT.⁸¹

Obviously this variation cannot be addressed by the general rules and it has to be set forth in individual protocols, with which each NME can conduct trade with other cps in accordance with GATT rules "to the extent possible" under its economic system.⁸² With this the possible "negative effects of freezing NMEs into a special, less favorable status" by inserting "fixed rules of general applicability" would be rectified. Thus greater decentralization and reliance on the market would be encouraged and rewarded individually.⁸³

4.4(2) MODIFICATION OF GATT RULES

Any approach outside the ambit of the GATT framework can not heal the inherent or internal diseases of GATT and cannot ultimately solve the problem of world trade integration. A better approach would be to find causes and location of weaknesses. One fatal shortcoming of GATT accommodations for integrating East-West trading systems is that they do not refer explicitly enough to the planning techniques in Eastern Europe.⁸⁴

As a remedying approach, the first effort should perhaps be made to introduce into the GATT provisions explicitly referring to the target-protected and state trading economies and recognizing those systems as alternative methods of organizing a country's foreign trade.⁸⁵

Indeed, it is both possible and desirable for GATT to develop Art. 17 on the basis of unfulfilled provisions along

the lines as suggested in the "Havana Charter" and relax some of its requirements with which NME obviously cannot comply.⁸⁶ Indeed, the arrangements for East-West trade in this respect are even less satisfactory than those offered by the American "Suggested Charter" and to some extent the Havana Charter of forty years ago.⁸⁷

To be specific, the GATT should incorporate new provisions on non-discrimination on plan targets.⁸⁸ It should also provide for a reciprocity arrangement along the lines of the U.S. "Suggested Charter" and should contain a clear set code of conduct on dumping, market disruption and safeguard clauses adapted to the state trading systems of the centrally-planned economies. Respective provisions should refer to planning techniques rather than rely on general statements and assurances.⁸⁹ This could be accomplished either by expanding and revising Article 17 of the GATT or by inserting additional part (for instance, Part V) dealing exclusively with NME membership at both procedural and substantive levels.

One alternative approach to import commitment could be based on the assertion that the import mark-up rates on trade between two or more state trading systems should be progressively reduced through target liberalization and domestic price adjustments.⁹⁰ Modifications along these lines could be introduced either by incorporating some new provisions into Article 24 or by inserting a waiver under the reduced import mark-up rate clause.⁹¹ However, this alternative approach itself has some constraints. It can be

weakened by variety of central planning measures.⁹² For example, sales of imports can be limited by issuing admission ticket and erecting restrictions on entrance.⁹³ In the case of China, this would run counter to the spirit of the current Chinese reforms because the reform will lead to elimination of government fixed targets for individual corporations. The Government has no reason to make such commitments to achieve volume of imports at a particular level.

A further approach would be to require NME members or applicants to increase transparency of their purchasing criteria and competitive bidding in domestic markets.⁹⁴

Since the absence of adequate information on the functioning of a NME's economic system has been a major barrier to its full acceptance into the GATT, the attention of the GATT should be shifted to include specific and detailed provisions aimed at increasing the transparency of the NMEs' economic and trade systems.⁹⁵ Under those improved transparency provisions all acceding NMEs and present NME CPs would have to provide data on, and/or submit to a working party examination of those specific areas particularly susceptible to manipulation for the purpose of influencing trade.⁹⁶ The information submitted is subject to supplement upon further request by GATT cps and Secretariat. Requirements regarding transparency of purchasing criteria and competitive bidding can be specified either in the GATT Government Procurement Code or in an annex to the Code.⁹⁷

In addition to this approach, in dealing with NME's state trading problems GATT may use the same "injury" approach as used in dealing with subsidy issue to overcome the dilemma with state-trading problems.⁹⁸ In its refined provisions, the GATT may first acknowledge state-trading system and regard it as a necessary instrument of trade control.⁹⁹ It would then renegotiate more detailed mechanisms for discouraging their use and minimizing "serious obstacles" to trade due to the operations of state trading and provide possible remedies for compensating "injurious effects" resulting from STEs.

In conclusion, all approaches are vulnerable. As circumstances change, the approach should also be changed. Any approach to NMEs' integration should be based on certain goal. The realization of the goal should be the touchstone of the viability of the approach.¹⁰⁰ In any event, one should note that the proposed new approaches might be used together with periodic consultations and provisional special safeguards as long as they are appropriate to reconciling diversifying trade systems and are able to increase the opportunity of solving the problem of global integration. There will be no single solution to the thesis problem. But decentralization coupled with transformation of command state trading system into loose state trading system might be the first best solution to resolving the problem of incompatibility between the GATT requirements on world trade and NME state trading systems.

4.4(3) "DECENTRALIZATION"-THE FIRST-BEST SOLUTION TO THE INCOMPATIBILITY?

Economic and trade reforms aim both at introducing market forces into the NMEs' domestic economy and decentralizing their foreign trade activities. This is the first-best solution to solving the problem of market access and incompatibility between NME and the GATT legal system. It is submitted that GATT rules are formulated exclusively along the line of the market economy ideology. The rules and principles are founded on sound assumptions. To change the original assumptions would dismantle the GATT rules. If NMEs can reform their economic system to be compatible with market principles, loosen command state trading links and allow free competition in purchases or sales and decentralize trading system, it is sure that the task of reconciliation and integration will be well completed.

The focus of the reforms should be on such areas of the incompatibility as their pricing system, state trading system in foreign trade, import and export control (licensing) system and tariff system. Decentralization of the planned economy with target-protected state trading system to be market economy with tariff-protected economy should be the general guideline and objective. In dealing with this the key issue is to determine what market conditions are needed in order to have NMEs conform with the GATT requirements, when it can be considered that there exists a market that can interact with those of FMEs' GATT CPs and furthermore what criteria should

be used to determine such a market.¹⁰¹ It is important that NMEs accept the established fundamental belief in the GATT that for the most part, the flow of goods among members is determined by principles of comparative advantage and commercial considerations.¹⁰² Supposing NMEs can do so, the differences between NME and FME in their economic systems will be only minor factors that should not discourage NMEs from participating in the GATT.¹⁰³

However, there are two obvious problems which may bother NME countries in joining the GATT. One problem lies in the lack of consensus among GATT members on the kinds of marketplace interventions by national governments that are deemed inconsistent with the development of a global market and the lack of a set of commonly agreed-upon rules.¹⁰⁴

Another more typical, perhaps common problem found in the NME is that NME countries lack institutions, habits, code of conduct and culture of a market system which may not be achieved within a few years. A comparison of Eastern European countries and China would show that it would be easier for East European countries to form market notion since they used to have western tradition. But for China, it will take a considerable amount of time to establish such institutions, habits and culture that would make it a "market economy" since China evolved from incredibly long period of feudalism.¹⁰⁵

It is recognized that the most important component of the reforms is to change the original pricing system. The focus of the Hungarian "New Economic Mechanism" was the freedom of

pricing in addition to the readjustment of its tariff system.¹⁰⁶ China is now aiming at replacing the long-adopted mandatory pricing with more of guidance pricing. It also wants to introduce market prices to regulate a high percentage of commercial transactions.¹⁰⁷ The purpose of massive on-going reforms is to decentralize once highly centralized foreign trade system.¹⁰⁸ It is also to introduce market forces into part of China's internal economy as regulatory forces.¹⁰⁹ As part of the foreign trade reform, tariff system is being codified and unified. Import licensing system of China will as a result of the reforms have a global and non-discriminatory nature towards each individual country.¹¹⁰

However, an essential and perhaps major part of the economy remains either centrally or locally controlled.¹¹¹ Moreover, the institutions and bureaucratic habits brought about partly by the socialist system and partly by traditional culture would make it hard enough to carry out the market principles enunciated in the GATT.¹¹² Also, many enterprises are still facing the crucial reality that freedom of pricing does not give them a direct access to the market due to the policy and legal limitations on the use of land, recruitment of employees, supplies of raw materials and financing facilities.¹¹³

This implies that the reforms in China must be continued in a more profound and broader fashion. It is contradictory and hardly understandable for China to introduce market principles into its economy and prepares to join the GATT but

keeps itself "a socialist dominant country."¹¹⁴ One cannot help wondering how much emphasis will be placed in the future on planing and how much on market principles.¹¹⁵ This ideological contradiction must be removed as soon as possible otherwise the reforms will be hindered. Moreover, as to the viability of "one state, two system" blueprint designed to be implemented after 1997 take-over of Hong Kong, time will tell. If this is manageable, it is likely that the same scheme will further be applied to Taiwan and ultimately extended to the mainland China.

Above all, the problem is that even China itself has perhaps, no idea about the direction in which it should go: either to go laissez faire or to maintaining its "centralism"; state-ownership or private ownership; "market" or non-market". The answer is yet to be found.¹¹⁶ In short, it would not be too much to say that assuming the fundamental tenet of comparative advantage and commercial behavior behind the GATT rules and principles is to be unchanged, the decentralization is by far the only and most effective option for reconciliation. Only through substantial decentralization can the problem of incompatibility and reciprocity be best solved.

4.5 OPTIONS FOR REGAINING CHINA'S GATT MEMBERSHIP

China has been interested in joining the GATT for years. But at least at the present stage China cannot make radical economic and political reforms to commit herself to accept

GATT rules to a full extent. Nonetheless, there still exist several options for reconciliation. As regards China's participation in GATT, the following options are worth considering:

(1) Either China reforms its economy and foreign trade system to such a degree that her economic system can be quite compatible with GATT as if it were a market economy; or

(2) Regardless of its deep-rooted MFN notion and liberalism, the GATT inserts special provisions suggested by "the American Charter" or "Havana Charter" to tolerate and compromise with state trading countries; or

(3) China accedes to GATT on the basis of special arrangement; or

(4) China gives up any attempt to join the GATT because of its inability or unwillingness to fully accept the market-based GATT regime and seek other viable avenues such as bilateral or regional trade arrangements; or

(5) Changes in both GATT's and China's trading systems or economic policies.

Among these options the first seems to be unrealistic at least in the near future. Even if China were willing to accept market ideology without reservation, it would take a considerably long period of time to complete. It is quite certain from its recent economic and political reform plan that China will only reform its economy to a model of so-called "planned commodity economy" which represents co-

existence of plan and market which is essentially a mixed system of state ownership and market regulation.

In considering the second option one may wonder how far or to what extent the GATT rules can be changed to reconcile with NMEs. As already stated, the major GATT rules and principles are rooted in market economies and are based on accepted assumptions of comparative advantage theory and fair competition doctrine among major trading partners namely, the U.S, Japan, the EEC, and some other middle-sized countries like Australia, Canada and New Zealand. To change GATT rules means to change their well founded assumptions. Indeed, GATT has changed some of its assumptions when imposing exchange obligations and "reciprocity" on LDCs. However, this change is only considered as an exception to MFN principle and is based on a new assumption that as long as there is a factual gap between LDCs and developed world, applying GATT rules would increase this gap and hinder their ability to expand exports. The benefit of this change is yet to be extended to NMEs.

As far as the third option is concerned, China as a major political and military power would think that participation on special terms would amount to accepting second-class membership.

The fourth option is actually no option. It implies that if neither China nor GATT changes, reconciliation is simply impossible. But it still gives China some alternatives including regional or bilateral arrangements through which it

can gradually succeed in participating in GATT-based world trade system.

The above analysis enables us to come to the conclusion that practically speaking, of the five options there are only two left for accommodation of NMEs' membership. One is the change of either GATT or the NME system. The other is both sides making moves to change. New adaptable rules to the NME is to be incorporated into the GATT legal framework as suggested earlier. The NME, on the other hand, is to be decentralized to the most compatible extent with the GATT rules and requirements. Once both sides make moves to change, as the case may be, their ingrained market-oriented or non-market state trading-oriented systems, a reconciliation may be achieved. It is expected that the GATT fundamental belief upon which its rules are formulated will not be modified to a large degree. Thus it would be reasonable to assume that the option of decentralizing NME system is by far the first-best approach for the NME countries to reconcile with the GATT legal regime.

FOOTNOTES

1 Comment: "Airbus and Its Ilk: Turning Nose at GATT" 20 *Harv. Int'l L.J.* 111, (1988), pp. 120-21.

2 *Id.*

3 *Id.* p. 121. ("Such a neutral standard would suit the political realities of today's world, where international tensions can be unnecessarily exacerbated by misunderstandings of the purposes behind countries' encouragement of domestic industries").

4 *Id.*

5 *Id.*; see also Bernier, "State Trading and the GATT" in *STATE TRADING IN INTERNATIONAL MARKETS* (Kostecki ed 1982), p. 252.

- 6 For a modified definition, see Comment, *supra* note 1, p. 122.
- 7 Roessler, "State Trading and Trade Liberalization", in *STATE TRADING IN INTERNATIONAL MARKETS* (Kostecki, ed. 1982) pp.280-81.
- 8 *Id.* at 281.
- 9 *Id.*
- 10 *Id.*
- 11 *Id.* at 280.
- 12 *Id.*
- 13 Kostecki, *East West Trade and the GATT System* (1978) (for the Trade Policy Research Center published by Macmillan), at 91.
- 14 *Id.* p. 91.
- 15 *Id.*, p. 127.
- 16 *Id.* p. 125. ("In that respect the three East European countries met the expectations of their GATT partners.") *ibid.*
- 17 *Id.* p. 125.
- 18 *Id.* p. 128.
- 19 *Id.* p. 95, 109. (discussing weakness of the Polish reciprocity formula); see E. Patterson, "Improving GATT rules for Nonmarket Economies" 20:2 *J.W.T.L.*185, pp. 188-89. (enumerating shortcomings of the Polish, Romanian and Hungarian import commitment). *ibid.*
- 20 Patterson, *ibid.*, at 188.
- 21 Kostecki, *supra* note 13, p. 95.
- 22 *Id.* pp. 95, 114-16. (" Even Poland's global import commitment, calculated in current dollar prices, has been deprived of any real significance - for two main reasons: (a) inflation, which increased substantially after Poland's accession; and, (b) reduction of value of the dollar in terms of other Western currencies.") *ibid.*, p. 114. See also Patterson, *ibid.*, at 188.
- 23 Patterson, *ibid.*
- 24 Kostecki, *supra* note 13, p. 95, 109.

- 25 GATT Doc., BISD, 18th Supp. 1972, p. 10. The deadline for a transitional period is as of Jan. 1, 1973 or any date at which Romania introduced a customs tariff.
- 26 GATT Doc. BISD, *ibid.*
- 27 E. Patterson, *supra* note 19, at 189.
- 28 *Id.*
- 29 *Id.*
- 30 *Id.*
- 31 *Id.*
- 32 Kostecki, *supra* note 13, p. 31. c.f. Yugoslavia's path to the GATT, *ibid.*, pp. 25-27.
- 33 *Ibid.*, pp.97-98. ("[D]ue to the political sympathy of the Western governments towards Hungarian efforts at economic decentralization", "the GATT countries accepted the tariff approach as valid for Hungary and concurred that reciprocity could be reached on the basis of a symmetric reciprocity formula as traditionally adopted in the negotiations of tariff-protected members of the GATT".) *ibid.*, at 31, 98. See also GATT Doc, BISD, 20th Supp. pp. 37-41.
- 34 Robert E. Herzstein, "China and the GATT: legal and Policy Issues Raised by China's Participation in the General Agreement on Tariffs and Trade" 18 *Law & Policy in Int'l Business*, at 388-89.
- 35 GATT Doc. L/6270 (Nov. 27, 1987), QUESTIONS AND REPLIES CONCERNING THE MEMORANDUM ON CHINA'S FOREIGN TRADE REGIME, (hereinafter *QUESTIONS & REPLIES*), pp. 9-36.
- 36 GATT Doc. L/6125, (18 Feb. 1987), "China's Status As a Contracting Party: Memorandum on China's Foreign Trade Regime," (hereinafter *MEMO*), p.12.
- 37 Herzstein, *supra* note 34, at 388.
- 38 *Id.* pp. 388-89. ("modified import commitment schemes").
- 39 *Id.*
- 40 Kostecki, *supra* note 13, pp. 110, 136-37, 144-45.
- 41 *Id.* at 109-10.
- 42 *Id.* p. 109.

- 43 *Id.* p. 110.
- 44 *Id.*
- 45 E. Patterson, *supra* note 19, at 189.
- 46 *Id.* at 190.
- 47 *Id.* pp. 190-91.
- 48 Kostecki, *supra* note 13, at 103, 135, and 139.
- 49 *Id.* p. 139.
- 50 K. Grzybowski, "Socialist Countries in GATT", (1980) 28 *J.W.T.L.* 539, pp. 551-2.
- 51 *Id.*
- 52 *Id.*
- 53 *Id.*
- 54 *Id.*
- 55 *Id.* p. 552.
- 56 Chen, Tungpi: "Are the Antidumping Laws of Canada and Other Western Countries Keeping Pace with China's Economic Structural Reform?", (1987) 19 *Law & Policy in Int'l Bus.* 717, at 725.
- 57 Kostecki, *supra* note 13, pp. 144-45; Patterson, *supra* note 24, pp. 190-91.
- 58 R.E. Herzstein, *supra* note 34, at 410.
- 59 *Id.* p. 411.
- 60 *Id.*
- 61 *Id.*
- 62 GATT Art. 28 *id.*
- 63 *QUESTIONS & REPLIES*, *supra* note 35, at
- 64 E. Patterson, *supra* note 19, at 203.
- 65 *Id.*
- 66 *Id.*, p. 203.
- 67 *Id.*, pp. 199-20.

- 68 *Id.*, at 203.
- 69 *Id.* p. 204. Bulgaria did acquire observer status in 1967, but it has been unsuccessful to date in efforts to join the Standards Code. It has not sought accession to the GATT itself. Note, however, that China has acquired observer status in several past GATT negotiations and is now anxious to regain the GATT membership in the current round.
- 70 Herzstein, *supra* note 34, at 412.
- 71 *Id.*
- 72 *Id.* pp. 412-13; GATT, Article 19.
- 73 E. Patterson, *supra* note 19, at 204.
- 74 Herzstein, *supra* note 34, at 413.
- 75 *Id.* at 413.
- 76 E. Patterson, *supra* note 19, p. 204.
- 77 *Id.* at 204.
- 78 *Id.* This idea was proposed by France, Austria, Brazil, and Sweden in 1950s.
- 79 The idea to accommodate NMEs by improving the GATT major trade rules was advanced to date known as "the Part V approach", under which rules regulating NMEs' state trading systems would be set out. Opponents to this novel approach argues vehemently that "the NME-versus-market economy is not a useful distinction a centrally-planned nonmarket economy is not the relevant characteristic as far as a country's status in the GATT is concerned." (see Patterson, *id.* p.204)
- 80 *Id.* 204-05.
- 81 See generally Li Chungzhou, "Resumption of China's GATT Membership" 21 *J.W.T.L* 25, 25-48 (1987)
- 82 E. Patterson, *supra* note 19, p. 205.
- 83 *Id.*
- 84 Kostecki, *supra* note 13, p. 135. Also, "one of the important omissions of the Polish and Romanian protocols for accession seems to be the lack of specific rules on the non-discriminatory operations of plan targets." *id.* p. 103.

- 85 Kostecki, *id.* p. 144.
- 86 *Id.*
- 87 *Id.*
- 88 *Id.*
- 89 Roessler, *supra* note 11, at 279-81.
- 90 Kostecki, *supra* note 13, p. 144; see also Herzstein, *supra* note 39, at 390, concerning "Restrict Mark-up on Import".
- 91 Kostecki, *id.*, p. 144.
- 92 Herzstein, *supra* note 34, at 390.
- 93 *Id.*
- 94 *Id.*
- 95 Patterson, *supra* note 19, pp. 199-201; also, Herzstein, *supra* note 34, p. 391.
- 96 For detailed discussion see Patterson, *id.* p. 200. (Areas in which information might normally be requested include: domestic price formation and its methodology, plan formulation and its content, trade statistics and other relevant data).
- 97 Herzstein, *supra* note 34, pp. 391-92.
- 98 Bernier, *supra* note 5, p. 252.
- 99 Comment, *supra* note 1, pp. 127-29.
- 100 Kostecki, *supra* note 13, pp. 144-45.
- 101 Herzstein, *supra* note 34, at 394.
- 102 *Id.*
- 103 *Id.*, pp. 395-96.
- 104 William P. Alford, "When China is Paraguay? - An Examination of The Application of the Antidumping and Countervailing Duty Laws of the United States to China and Other 'Nonmarket Economy' Nations", 61:79 *Southern California L. Rev.*(1987), 79, at 130.
- 105 Herzstein, *supra* note 34, at 396.
- 106 Kostecki, "Hungary and GATT" 8 *J.W.T.L* (1974) 401, at 406.

- 107 GATT Doc. L/6125, (18 Feb. 1987) (China's Status As a Contracting Party: Memorandum on China's Foreign Trade Regime), at 6-7.
- 108 Zheng Tuobin, "Planning Further Foreign Trade Reforms" *INTERTRADE*, (Oct. 1984), at 24.
- 109 *Id.*
- 110 *Id.*
- 111 Herzstein, *supra* note 34, pp. 395-97; see also QUESTIONS & REPLIES, *supra* note 35, pp. 22-24.
- 112 Herzstein, *id.*, p. 396.
- 113 *Id.*
- 114 *Id.*
- 115 *Id.*
- 116 See generally Halpern, China's Industrial Economic Reforms, 25 *ASIAN SURV.* 998 (1985) (Reforms have come and gone as the Chinese government has searched for the proper balance between state planning and economic incentives.) *Id.*, p. 998.

PART FIVE: CLOSING REMARKS AND PERSPECTIVES

To integrate NME state trading systems into the old-fashioned GATT legal framework is by no means an easy task. Because of the inherent incompatibility between state trading systems of the NMEs and private trading system under the GATT, both will be simply irreconcilable if neither NME system nor the original GATT regime is to be changed.

As the review of the GATT experience with the Eastern Europe's accession to the GATT has shown, there has been considerable difficulties in using the original framework of the GATT to integrate state-trading systems in NMEs especially command state trading system into the GATT trading rules and systems. The fundamental difficulty lies in the fact that NMEs' governments could not possibly give up control on foreign trade. Their import and export are not simply guided by "commercial considerations" nor determined by the relation of domestic prices to foreign prices but by government direction and quantitative restrictions. Thus, tariffs could not possibly be operated as the only economic lever to influence the choice between importing and not importing even if tariffs are to be applied on MFN or non-discriminatory basis.

In the light of such incompatibility, it is certainly frustrating to consider the possibilities of reconciliation. However, the possibilities of reconciliation lie in a very

fundamental assumption. They will be reconcilable if either NMEs' state trading systems or the original GATT assumptions framing its major rules are to be changed. Accordingly, the main task of resolution is to illustrate how and to what degree they have to be modified. The easiest way towards reconciliation and integration is a full decentralization in the state trading systems. This is possible but takes time. The possibility is limited by the political will of NME governments. The possibility will fluctuate as their political will changes from time to time.

Also, the policy of decentralization in NME may be inconsistent. And inconsistency will certainly undermine the expectations of the GATT countries. The dilemma is that if the stage of decentralization has not been completed, there will be no full integration. This was shown in the U.S. trade policy for the accession of Hungary, Poland and Romania to the GATT. The U.S. did not extend or apply its MFN treatment to these countries until late in 1970s. Moreover, QRs were still maintained by most of Western European countries after the Eastern bloc's accession. The GATT has not solved the integration legally within its original framework. Rather, it was solved temporary on a country-by-country and pragmatic basis. It is certainly worthwhile to seek the other avenues towards reconciliation outside the GATT framework. This, however, will not lead to a genuine and complete integration. At best, it is only a means of reconciliation and not integration. Reconciliation of different systems may be the

first step to achieve at least partial integration. Full integration means global integration. Within such integration one finds a single trading system under which all participating countries in the GATT conduct their trade with one another. With regard to a co-existence of diverging trading systems, this ideal will not be accomplished in a short-run.

In any event the accession of socialist countries to GATT is a realistic step which may eventually bring about their integration into a world trade system.¹ But this is only the first step. Each case of accession was an independent experiment and only the future will show which method will prove best at liberalizing trade between free-market economy and socialist economy.²

The integration is not only time-consuming but also subtle due to the fact that NMEs' accepting the GATT system would be limited by the ability to afford economic cooperation with free market economies.³ Their basic common aim is to develop their economies by borrowing foreign capital and advanced technology to increase exports and have more hard currency reserve. Stressing industrial and high technology production would frustrate those goals.⁴

Recognizing the varying political and economic systems and understanding the NMEs' problem with free competition with minimal government intervention, the framework of the GATT allows various levels of participation in the program of free trade.⁵ This is out of political considerations rather than of

pure commercial concern. The GATT's admittance of four socialist countries (Romania, Poland, Yugoslavia, Hungary in addition to the original two) into its framework was more out of political expectations rather than of pure trade policies.⁶ Obviously, such political expectations widened NMEs' participation in the GATT. And the NMEs' broader participation would in turn increase world prosperity and economic well-being. World prosperity and economic well-being are eventually the best guarantee of world peace and security.⁷ Grzybowski wrote:

"Economic development and world prosperity are the best guarantee of peace; trade, one of the most important factors in raising the standard of living, responds to a political climate which promotes the sense of security."⁸

Indeed, as many GATT members are aware, NME's accession to GATT have brought and will continue to bring benefits to the rest of the World.⁹ In the words of Prof. John Jackson, "there is more to be gained by full and universal participation in the international discussions of economic affairs than there is by the exclusion of certain states".¹⁰ Admittedly, NME membership and their continuous participation in GATT-sponsored multinational negotiations will definitely help to achieve the goal of a single world trade system and will increase world peace and prosperity. Economic unity will be the first and indispensable step to fulfill political or ideological unity which was once the dream and aspiration of the United Nations and ITO-based multilateralism.

Unfortunately, the leaders of the West namely, the United States, Japan and the European Economic Community (EEC) are still distrustful of the socialist state trading economies.¹¹ They simply lack political will and confidence in fully integrating NMEs into the GATT. This lack of political will and confidence is confirmed by many Western writers who regard the issue of integration simply impossible as long as the state trading system remain prevalent in the socialist economies.¹²

If we appreciate the extent to which the GATT has departed from market principle ideals to reach a framework that facilitates trade, the task of creating new rules for international trade that accommodate all nations will become more realistic.¹³

FOOTNOTES

¹ Grzybowski, "Socialist Countries in GATT" 28 J.W.T.L 539 (1980), at pp. 551-52.

² *Id.* p. 552.

³ *Id.*

⁴ *Id.*

- 5 *Id.* Indeed, GATT seems to provide a framework for trade cooperation of a least three groups of countries: (i) highly industrialized economies, which can meet the challenge of free trade and the international division of labor with no prejudice to their living standard; (ii) the developing economies, which need assistance, and are unable to reciprocate fully the advantages of admission to GATT on terms of equality (see Articles 18 and 36-38); (iii) finally, state trading economies which are not, due to their social, political and economic order, fully compatible with the market-type GATT system and thus unable to be fully integrated into the world trade mechanism.
- 6 *Id.*
- 7 *Id.* p. 553.
- 8 *Id.*
- 9 Frank Stone, *Canada the GATT and the International Trade System* (1984), p. 167.
- 10 J.Jackson, *World Trade and the Law of GATT* 329-32 (1969), at 777.
- 11 Grzybowski, *supra* note 1, p. 554. Yet, it must be recognized that trust is a condition related primarily to the conduct of governments in international relations. *Ibid.*
- 12 Jackson, *supra* note 10, p.1179. ("many of the GATT rules make sense only in the context of such a market system, since they restrict the types of regulations which governments can impose on international traders, but do not purport to regulate the traders themselves."); K.W. Dam, *The GATT Law and International Economic Organization* (1972) ("[The GATT tariff] system presupposes that importation and exportation are handled by private firms which, stimulated by private motives, are guided by commercial considerations...when one considers state trading, the underlying assumption of the GATT system is itself no longer applicable"), *id.*, p.318; K. Kennedy, "The Accession of the Soviet Union to the GATT" (1987), 21 *J.W.T.L.* 23 (with respect to the Soviet accession to GATT, "unless the Soviets are prepared to make gradual but nevertheless dramatic reforms in their economic system, the answer is certainly 'no'"), at 33.
- 13 William P. Alford, "When Is China Paraguay? An Examination of the Application of the Antidumping and Countervailing Duties Laws of the United States to China and Other 'Nonmarket Economy' Nations" 96 *Southern California Law Review* Vol. 61:79, at 132.

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