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WORKING PARTY ON THE ACCESSION OF CHINA

Communication from the International Monetary Fund

The following communication¹ has been received from the International Monetary Fund with the request that it be circulated to members of the Working Party.

GROUPE DE TRAVAIL DE L'ACCESSION DE LA CHINE

Communication du Fonds monétaire international

Le Fonds monétaire international a fait parvenir au Secrétariat la communication ci-après¹, en demandant qu'elle soit distribuée aux membres du Groupe de travail.

GRUPO DE TRABAJO SOBRE LA ADHESIÓN DE CHINA

Comunicación del Fondo Monetario Internacional

Se ha recibido del Fondo Monetario Internacional la siguiente comunicación¹, con el ruego de que se distribuya a los miembros del Grupo de Trabajo.

¹English only/anglais seulement/inglés solamente.

Statement of the Representative of the International Monetary Fund
to the Working Party on China's Accession to the WTO

22 March 1996

Mr. Chairman,

The Managing Director of the International Monetary Fund would like to convey a message regarding the clauses on exchange arrangements in the draft Protocol on China's accession to the WTO. I would request that this message be placed on the record of today's meeting of the Working Party. I am also circulating to the Working Party the attached staff statement to the Executive Board of the Fund (BUFF/95/23), which was made on the occasion of the 1995 Article IV consultation with China, and which explains our concerns in more detail.

The Managing Director's message is as follows:

"The Fund fully shares the objective of members of the Working Party of assisting China in moving to an open exchange and trade system. We agree that complementary exchange and trade liberalization will be in the interests of China, its trading partners, and the world community. Let me also say that we understand the intention of the draft Protocol in wishing to ensure that exchange measures are not used to frustrate trade agreements.

China has been steadily liberalizing its exchange system. The assessment of the recent Article IV consultation mission to China, whose report is expected to be discussed by the Fund's Executive Board on 1 April, is that in practice China is already close to achieving current account convertibility. The authorities are undertaking a review of existing foreign exchange laws and regulations, and the staff has emphasized the importance of bringing them into line with practice and removing the remaining restrictive features. The Fund staff is working actively with China on the reform of its exchange system as a prelude to its acceptance of the obligations of Article VIII, Sections 2, 3 and 4 of the Fund's Articles of Agreement in the near future.

However, inclusion of exchange provisions, as currently drafted in the draft Protocol, raises serious concerns. These provisions give rise to important questions regarding their consistency with the rights and obligations of Fund members under the Fund's Articles, and with established practice for dealing with the exchange systems of common members. Moreover, these provisions risk inconsistency with Article XV of GATT (1994), Article XI of the GATS, and principles set forth in the Declaration on the Relationship of the World Trade Organization with the Fund. We suggest that the draft Protocol drop all references to exchange measures under Fund jurisdiction. Alternatively, we would be willing to cooperate with the Working Party to develop a formulation on exchange arrangements in the draft Protocol that would deal with our concerns. We would also be willing to provide to the Working Party regular briefings on the status of China's exchange regime."

Statement by the Staff Representative on Fund/WTO Jurisdictional Matters at the Discussion
of the Article IV Consultation with the People's Republic of China
Executive Board Meeting 95/27, 22 March 1995

Traditionally the Fund and the GATT have promoted external liberalization in their respective areas of jurisdiction - exchange measures in the Fund and trade measures in the GATT. In the case of China, the staff and Board of the Fund have encouraged China to liberalize its exchange system, and with considerable success. China is negotiating a protocol on its membership in the WTO, and a list of tariff and trade concessions. At issue, however, is the unprecedented inclusion in the draft Protocol on China's membership of the WTO of obligations relating to its exchange system.

Specifically, the current draft provides:

- "1. China shall not use foreign exchange controls or restrictions to regulate the level or composition of trade in goods and services. China shall, by [x date], establish a unified foreign exchange market, remove all restrictions on access to this market and eliminate guidelines specifying the priority uses of foreign exchange.
2. China shall, by [x date], bring its foreign exchange regime into conformity with obligations under Article VIII of the IMF. Individual requests of foreign exchange for current account transactions shall not be subject to any form of approval, and the issuance of a letter of credit or a bank guarantee upon presentation of an invoice shall not be subject to any form of governmental restriction.
3. China shall not resort to laws, regulations or other measures, including requirements with respect to contractual terms, which have as their object or effect to influence foreign exchange earnings or expenditures."

Leaving aside questions of the precise meanings of these commitments (which, as phrased, create certain ambiguities), they do establish obligations in the area of exchange restrictions. If China were to violate these obligations, other WTO Members might eventually be authorized to take retaliatory action.

There is no question that the Fund and the parties negotiating with China in the WTO framework are seeking the same goal: a durable liberalization of China's restrictive system and its integration in the world economy. However, the Fund staff is concerned that serious problems could arise from the way this draft Protocol affects the established division of responsibilities between the Fund and the GATT, now WTO. Some of these concerns are elaborated below.

1. Article XV, paragraph 9 of the GATT 1994 recognizes the right of a WTO Member that is a Fund member to maintain exchange controls or restrictions in accordance with the Fund's Articles. Fund members have not in the past been required to waive this right as a condition for accession to the GATT.
2. In this respect, it may be noted that, for a non-member of the Fund applying for WTO membership, Article XV, paragraph 7 of the GATT 1994 on special exchange agreements would explicitly prevent the imposition of obligations in exchange matters generally more restrictive than those imposed by the Articles of Agreement of the International Monetary Fund on members of the Fund. The inclusion of obligations on exchange restrictions in the Protocol could lead to a case where a non-member of the Fund is treated more favourably than a Fund member.

3. A Ministerial Declaration in the Final Act on the WTO's relationship with the Fund calls for the continued application of Article XV, which recognizes the Fund's jurisdiction over exchange matters, and the WTO Agreement calls for cooperation with the Fund with a view to achieving greater coherence in global economic policy making. It is particularly important at this juncture, with the Uruguay Round Agreements coming into effect, to give substance to these provisions.

4. The draft Protocol would create an unfortunate precedent, which would conflict with the principle of uniformity of treatment under the Fund's Articles by establishing two classes of Fund members in respect of their exchange regimes.

5. Beyond jurisdictional issues between the Fund and the WTO and the particular issue of China, the draft Protocol could have implications for the Fund as a financial institution. The Fund makes its resources available to its members in case of balance-of-payments need. In this respect, the Fund should be able to exercise its jurisdiction under its Articles in order to effectively protect its resources, including through temporary approval of exchange restrictions.

The incorporation of the exchange clause (as currently drafted) in the Protocol on China's membership in the WTO would have a number of effects. Firstly, it would mean that a member enjoying its rights under the Fund's Articles could be subject to a punitive action under the rules of another international body. It could also mean that this Board's judgement on a member's exchange system could be disregarded by the judgement of WTO bodies. This is not consistent with the established pattern of jurisdiction between the Fund and the GATT.

An opportunity for a discussion of the substance of these issues relating to the jurisdictions of the Fund and the WTO might be a future meeting of the Committee on Liaison with the CONTRACTING PARTIES (CGATT).