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Gregory L. Waddoups
Utah State University

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The Soviet Union and the GATT:
An Impossible Combination?

Gregory L. Waddoups
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Thesis Advisor
Dr. Carolyn Rhodes

PREFACE

In considering the relationship between the General Agreement on Trade and Tariffs and any given state, one must examine not only the economic reasons for acceptance and participation, but also the political. This is especially true when dealing with the Soviet Union. In researching this topic, I have found that economics and politics are deeply interwoven into the fabric of international dealings with the Soviets on any level and at any given time.

Soviet participation in the GATT goes back to the very beginnings of the Bretton Woods institutions and of the International Trade Organization. While this participation runs contrary to our "Cold War" ideology, during World War II it was very much in the Allies best interest to assure Soviet participation.

Following the fall of the Berlin Wall and the implementation of Mikhail Gorbachev's perestroika and glasnost, it has once again become economically and politically in the West's best interest to include the Soviets in the economic order. However, tensions left over from the "Cold War" have not dissipated easily and many, including the U.S., are precluding the accession of the Soviets to the GATT. This is wrong. The Soviet Union and the GATT are not technically/economically opposite institutions, and therefore political attitudes should change to include the Soviets within the Western "circle of friends".

**THE INTERWAR PERIOD
AND
THE CREATION OF
INTERNATIONAL ECONOMIC ORGANIZATIONS
(1934-1947)**

In the years immediately following World War I, trade was characterized by an economic anarchy initiated by countries seeking to export their post-war unemployment and defend themselves against external shocks. These desires, coupled with intense feelings of nationalism and isolationism, led to the wide-spread implementation of exchange manipulation and multiple rates, import barriers, restrictive bilateral agreements, and high tariff rates (McCormack 19, Morrison 3-4). These self-centered, beggar-thy-neighbor economic policies helped lead to the world-wide depression of the 1930's (Cooper 666, Culbert 382) and are believed to be the economic catalysts of World War II (Kostecki 1).

The economic decline attributed to these practices also served as the impetus behind today's international economic organizations. In 1934, following a 70 percent decline in the gold value of exports in just four years, the U.S. was ready to accept a rethinking of its foreign trade policy (Morrison 3). This new outlook, developed in the 1934 Reciprocal Trade Agreements Act, emphasized the expansion of American exports over imports (Culbert 383), gave the President authority to enter into reciprocal trade agreements with foreign governments to reduce tariffs, and incorporated Most Favored Nation (MFN) doctrine "where any bilateral tariff reduction negotiated by the U.S. extended to all MFN countries" (Morrison 3-4).

Even though the Reciprocal Trade Agreement was an economically advantageous move away from the U.S.'s previous autarkic position, it still had problems, the biggest being that the Agreement provided no protection against third countries "enjoying the MFN benefits of a particular bilateral trade agreement without making concessions of their own" (ibid). In order to eliminate this freeloading, the U.S. began to turn to a multilateral form of trade negotiations. This trend was enhanced by the realization (during World War II) that international economic cooperation is a necessary ingredient for world peace (ibid).

Due to their desire to avoid previous economic problems and increase the use of multilateralism, the Americans and the British began to lay the groundwork for a post-war international economic community (Culbert 382, Kostecki 1). In 1939, work was begun on the Atlantic Charter, a document which was to serve as a backbone for U.S. and British trade relations. This document, much to the chagrin of the British (due to their practice of Imperial Preference), prescribed the use of a mild multilateralism to guide subsequent efforts at post-war reconstruction (Culbert 386).

In 1941, U.S. and British talks led to the creation of a Mutual Aid Agreement governing the provisions of Lend-Lease supplies to Great Britain and establishing commitments on post war trade policy. Article VII of this agreement called for

action by the United States of America and the United Kingdom, open to participation by all other countries of like mind, directed to the expansion, by appropriate international and domestic measures, of production, employment and the exchange and consumption of goods ... to the elimination of all forms of discriminatory treatment in international commerce and to the reduction of tariffs and other trade barriers (Culbert 387).

In accordance with this statute and as envisioned by U.S. Secretary of State Cordell Hull, proposals concerning the world-wide elimination of discrimination and the lowering of tariffs were initiated in 1942. These plans served as a catalyst for the creation of an International Trade Organization (ITO). E.F. Penrose, an economic adviser at the American Embassy in London during the early 1940's, wrote, "if any one event can be designated as marking the origin of the International Trade Organization, it took place at Whitehall [where James Mead, a member of the Economic Section of the War Cabinet Secretariat in the British Government, worked on his proposal for a post-war liberal trade regime] in the latter part of 1942" (Culbert 388). Talks between the U.S. and England continued into early 1945--stalled over American insistence that Britain give up its policy of Imperial Preference--and in the end,

the agreed tariff reducing process consisted of a series of bilateral negotiations taking place more or less simultaneously between a group of countries which would then extend their tariff reductions via the MFN principle (Culbert 396).

In the years that followed, numerous conferences were convened under the auspices of the United Nations (U.N.) in an attempt to draft a Charter for the ITO on the basis of what had already been agreed upon by U.S. and British planners (ibid). The Charter's key principles included U.N. affiliation to insure global participation and a goal to increase international trade through a lowering of tariffs. The primary tasks of the ITO were to monitor commercial policy, ensure full employment and balanced economic activity, assist in economic development and reconstruction, make certain the abolition of restrictive business practices, regulate capital flows, and monitor and facilitate

intergovernmental commodity agreements. "In short, it was to function very much like an international trade court" (van Brabant 9).

However, in late 1946 and early 1947 as debate continued on the establishment of the ITO, the nations involved began to change their internationalist leanings. Even US politicians and economists were in disagreement over whether to seek implementation of the Havana Charter [ITO] (van Brabant 9 1988). This uncertainty led to a slow down in discussions, and by the time the charter was drawn up, multilateral tariff negotiations under the general agreement had already begun (Morrison 4).

The General Agreement (GATT) was initially established to serve as a provisional agency which would be integrated into the ITO upon its ratification. However, opinion in the U.S. turned against the ITO and it became clear that defeat was inevitable. Therefore, the charter was never placed before the U.S. Senate for ratification and the GATT was, by default, left as the chief instrument for regulating international trade (Culbert 396, Morrison 4, Sokil 271).

Even though the original purpose of the General Agreement was to guide international commercial policy until the ratification of the ITO (Morrison 4) and therefore lacks any organizational and procedural provisions (van Brabant 10), it was ratified by 23 countries in October 1947 (Culbert 381) as *the* document outlining accepted negotiation procedures to remove tariffs and other obstacles to international trade (Cooper 666). The guiding principles of the GATT include most of the commercial policies of the ITO charter and establish a stable basis for trade and the settlement of disputes (Morrison 4).

The requirements for GATT membership can be broken down into four major areas: non-discrimination, reciprocity, transparency, and the use of tariffs.

NON-DISCRIMINATION

The GATT assures that a government may not, in principle, discriminate as to the origin or destination of its traded goods (Kostecki 35). This is implemented through the use of the MFN principle first established in the 1934 U.S. Reciprocal Trade Agreement Act. The GATT states 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 (Kostecki 35).

This insures that any concession granted to one member of GATT must be extended to others (Sokil 278).

RECIPROCITY

Reciprocity in the GATT gives assurance that every participating government will maximize its gains from trade cooperation. This is assured because trade negotiations within the GATT takes place between two countries and will be agreed upon only when the benefits are at least equal to costs for each party (Kostecki 37). The original GATT reciprocity formula was symmetric in nature and relied on the exchange of concessions of an identical nature--tariff reduction for tariff reduction (Kostecki 40).

TRANSPARENCY

In order to accomplish the lowering of tariffs and other international trade barriers, GATT countries must provide accurate information about their economy to other

members (Sokil 278, Kostecki 43). Without this information, it is very difficult to ascertain the openness of markets and the degree of tariff concessions that should be made to ensure equal access.

TARIFFS

In order to facilitate a meaningful reduction of trade barriers, the GATT assumes a direct link between foreign and domestic prices. This being so, its members are expected to control trade indirectly through prices rather than directly, by using subsidies, quotas, and other non-tariff trade barriers (Sokil 271). Due to the non-discriminatory nature of tariffs, the GATT turned to provisions requiring that where protection of domestic industries is necessary, it should be given exclusively through the use of a customs tariff (Kostecki 41).

During the years of 1936-1947 the world's perception of economic integration had changed dramatically. Out of anarchic, self-centered economic policies arose problems that could be solved only through the implementation of mutual economic policies. It was out of this desire, and the downfall of the ITO, that the GATT emerged to govern the new economic order.

**SOVIET PARTICIPATION
IN THE
INTERNATIONAL ECONOMIC ORGANIZATIONS
(1942-1946)**

The Soviet Union kept close watch over the creation of the post World War II international economic order. It was keenly interested in the international economic conferences and took an active role in the early developments of the Bretton Woods Institutions¹ -- the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development (IBRD) (Sokol 277, Kostecki 2). Moscow even supported the Western proposal of creating the ITO and was expected by the West to participate in this organization -- evidenced by the framer's intent that the Soviets occupy one of the eight permanent seats of the Executive Board of the ITO (van Brabant 6).

The Soviet's desire to participate in these economic institutions, coupled with American and British aspirations to create a truly international organization (Sokol 277), led to a Soviet-friendly drafting of the American "Suggested Charter" of the ITO. This document, which provided the basis for discussion at the 1946 London Conference, included "provisions directly relevant to the Soviet monopoly of foreign trade and was extremely tolerant of economic centralism" (Kostecki 2).

Technical arrangements were also provided within the Suggested Charter to insure compatibility between the goals of trade expansion and non-discriminatory treatment and the Soviet's state monopoly of foreign trade and payments. The key provision stated that a state-trading country

shall promote the expansion of its foreign trade with the other members in consonance with the purpose of the charter. To this end such member shall

negotiate with the other members in an arrangement under which, in conjunction with the granting of tariff concessions...and other benefits..., it shall undertake to import in the aggregate over a period products of the other members valued at no less than an amount to be agreed upon. This purchase agreement shall be subject to periodic adjustment (van Brabant 14).

The provision further set out four points to deal with the unfair advantages granted a state-trading country, such as the Soviet Union, by its participation in an international trade organization which uses the monitoring and reduction of tariffs to increase trade. First, in order to preclude the manipulation of trade for political purposes, a state trading country must conduct its foreign trade in accordance with commercial and non-political considerations. Second, the ITO provided a method to prevent a state-trading country from effectively using export subsidies or high import tariffs in ways prohibited by the charter. Third, in order to work toward the elimination of quantitative restrictions, governments were prevented from using state trading to circumvent bans on quotas. Fourth, the charter holds state enterprises accountable to its provisions curbing restrictive cartel practices (van Brabant 14).

The inclusion of these "custom made" provisions in the Draft Charter confirms the desire of Western governments to include the Soviets in the new economic order (the Soviet Union and Mongolia were the only CPE's at that time). In addition, the reservation of one of the ITO's permanent seats for the Soviet Union shows that the West, due to the Soviet's active participation in the Bretton Woods conferences and the perception that Moscow was in favor of the ITO, expected the Soviets to participate fully in the post-war economic institutions. However, this was not to be the case.

**SOVIET REJECTION
OF THE
INTERNATIONAL ECONOMIC INSTITUTIONS
(1946-1985)**

Following the conclusion World War II in both Europe (May 1945) and Japan (September 1945), Soviet-Western relations deteriorated rapidly and on 31 December 1945 Vyacheslav Molotov, the Soviet People's Commissar for Foreign Affairs, sent a decree to the U.S. stating that,

The Soviet Government does not find it possible at this time to sign the draft agreement drawn up at Bretton Woods concerning the creation of an international monetary fund and an international bank for reconstruction and development. The Soviet government finds it necessary to subject the questions touched upon in these drafts to further study in the light of those new conditions of the economic development of the world which are forming themselves in the post-war period (State Department 1388).

Whether this cooling of relations had been premeditated² or was the result of a Soviet perception of Western hostility³, it definitely signalled the end of universal international participation in the post war world and the beginning of the Cold War (initiated in February 1946 by Stalin's speech to voters before the Supreme Soviet and acknowledged in March 1946 with Winston Churchill's "iron curtain" speech).

In early 1946, following a Soviet concession to sign the Bretton Woods Articles of Agreement, it appeared that once again the Soviets were ready to participate. However, all hope was dashed as the Cold War accelerated and the Soviets failed to ratify the accord at the First Governors Conference in March 1946. This precluded them from any participation in the IMF and the World Bank (Sokil 270, van Brabant 11).

Furthermore, following their non-participation in the 1946 London Conference⁴

(in which debate centered on the American Suggested Charter of the ITO) the Soviets were not invited to the GATT initiatory talks at the Geneva Conference in mid-1947 (ibid). Thus, within a period of two years, the Soviets had totally alienated themselves from all international economic organizations.

Although Moscow has never given an official explanation of why it did not follow through with these organizations, Western analysts have attributed Stalin's apparent change of heart to several factors. These can be broken down into two general categories--politics and economics

POLITICAL REASONS FOR NON-PARTICIPATION

In the early post-war period, Soviet foreign policy was dominated by a fear that America (the only industrialized country not ravaged by World War II) would seek economic and political domination of the post-war world (Kennedy 28, 24). Moscow, therefore, saw the Bretton Woods institutions and the ITO/GATT as an opportunity for the U.S. to use the principles of freer trade and increased investment opportunities to further its goal of global hegemony (van Brabant 11, Kostecki 8) at the expense of the Soviet Union (Sokil 279) and less developed countries (Kostecki 22).

This fear, based on the American/British origins of the economic institutions and reinforced by the influence the U.S. wielded in the non-ratification of the Soviet-friendly ITO, was intensified after a US led motion to rejection Moscow's request for a substantial war recovery loan (Sokil 271). Furthermore, a misunderstanding concerning the reparation payments due the Soviets from defeated Axis countries led to hostile feelings when Moscow was not allowed to extract the payments it thought was due (van Brabant

11).

From a Soviet perspective which anticipated U.S. hegemony, any participation in the multilateral trading system carried with it a danger that the U.S. might expand economically and politically into the Soviet sphere of influence. This was undesirable given the Soviet desire to create a buffer zone of protection from another invasion. In fact, in order to gain and preserve this buffer, Stalin created the International Socialist Trade Unions and the Council for Mutual Economic Assistance (CMEA) directly after rejecting the Bretton Woods institutions (Sokil 279). Furthermore, ideas common to the post war institutions such as non-discrimination and multilateralism would not allow the Soviets to develop a system of bilateral economic agreements with Eastern Europe (Kostecki 22, van Brabant 11). This would undermine their economic control, and thus, their power to preserve a buffer in these areas.

The Soviets also believed that their participation in an otherwise market oriented institution would necessitate their achieving only second class status within the economic organization (Sokil 279). Following World War II, the Soviet Union experienced an intense surge of nationalism, due in part to their "single handed" defeat of the Nazis, which would not allow them to be content with a second best alternative.

In the end, the political ramifications of the institution's Western origins were too overwhelming for the Soviets. The fear of Western, and especially American, dominance within Moscow's sphere of influence weighed heavier than any benefit that may have been gained through participation.

ECONOMIC REASONS FOR NON-PARTICIPATION

The Soviet Union's economic reasons for withdrawing their participation from all forms of universal economic institutions are grounded in three ideas: first, a perception that the differences between Moscow's CPE and GATT's slant towards market driven economies would create more problems than benefits; second, the Soviet belief that capitalism was going to fail, resulting in economic chaos; and third, Moscow's concern that participation in a globalized market system would subject the Soviet economy to world economic problems.

Even with the concessions granted CPE's in the American Suggested Charter for the ITO, the Soviets felt that requirements for multilateralism and non-discrimination, reciprocity, transparency, and its emphasis on the use of tariffs were not compatible with their state trading system. Western insistence on multilateralism and non-discrimination contradicted the country specific planning program used in the Soviet foreign trade sector (Kostecki 22) and impede using trade relations as a political negotiating tool.

The Soviets also believed that reciprocity is an inappropriate principle for the post-war world of have and have-not countries (Kennedy 28, van Brabant 11). They believed that protectionism was necessary for their own industrialization (Kennedy 28) and that a multilateral trade order went against the interest of small and intermediate traders such as themselves (Kostecki 22).

The insistence of the post-war institutions on transparency also created a rift between the Soviets and other Western governments. Stalin, because of his penchant for privacy and belief that the West could use that information to down-grade the Soviet Union, did not want to divulge economic information (Sokol 279) including the size of his

country's gold reserves (Hewett 388).

The Soviets, due to their centrally planned pricing structure, do not use a discernable system of tariffs to protect domestic industries. This makes it very difficult for other countries to gain meaningful concessions from the Soviets to off-set their own tariff reductions.

Moscow's belief that capitalism was destined to fail, the second economic reason behind the Soviet withdrawal, led to uncertainty regarding the stability of a market-based trading organization. Additionally, following the anticipated economic downfall of the Western countries and the reemergence of world-wide unemployment and overproduction the Soviets felt that they would be able to obtain favorable loans and cheap supplies to boost their drive towards industrialization (Kostecki 22).

This belief in the inevitable decline of capitalism also prompted a Soviet desire to insulate its economy from the severe economic depression expected to rock the post-war period (van Brabant 11, Sokil 279). In order to accomplish this, foreign trade during the Stalinist period was treated as a necessary evil. Soviet politicians and central planners avoided the international market because they could not control it. This lack of control led to worries that an open Soviet economy may give rise to unemployment and inflation. Because of these concerns, the Stalinist system promoted autarky and took little advantage of gains from trade (Gardner 8).

Moscow's withdrawal from the planning stages of the IMF, IBRD, and ITO/GATT not only affected the world economic system at that time, but also influenced changes in the final drafts of these institutions. The 1946 American Suggested Charter

contained specific provisions pertaining to the integration of non-market economies into the international system (van Brabant 13). While these allowances were carried over to the Havana Charter (ITO), the Soviet's absence at the 1946 London Conference and disregard of subsequent international meetings rendered impossible any constructive discussion concerning the place of state trading monopolies in the multilateral system (Kostecki 2).

Therefore, the GATT does not include any provision to help NME's assimilate into its auspices (van Brabant 13, Sokil 277). The only surviving definition of a state trading enterprise in the context of the GATT, as ratified in 1947, addresses an enterprise that operates within free market economies. Thus, the document is concerned only with an occasional instance of state trading within those economies, not as practiced in CPE's.

Still, as a result of Soviet participation in the discussions until the first Board of Governors meeting of the IMF in March 1946, the international economic institutions contain provisions for state trading (van Brabant 11). Granted, these measures are limited, but it is through these exceptions that Eastern European countries have been able to accede into the GATT.

**THE SOVIET ACCEPTANCE
OF MULTILATERALISM
AND
EASTERN EUROPE'S ACCEPTANCE
OF INTERNATIONAL ECONOMIC ORGANIZATIONS
(1955-1986)**

Following Stalin's death in March of 1953 and the election of Nikita Krushchev as the First Secretary of the Central Committee, East-West relations experienced a significant economic and political thaw. This came about not only because of the change in leadership, but because the Soviets had firmly established their dominance over the Eastern Bloc and their legitimacy as a political and military power. This betterment of relations, combined with Moscow's new emphasis on economic policy objectives such as developing technologically intensive industries and raising the standard of living, led to an increase in East-West trade activity. These changes of political and economic attitudes then served as the impetus for the Soviet Union to once again experiment with the international accords governing trade.

The first step in initiating participation in international economic institutions was cleared in 1955 after the Soviets recognized that an international order promoting freer trade, non-discrimination, and multilateralism was in their best interest and that, in fact, medium traders such as themselves derive the most important economic advantages from the system. The Soviet proclamation stated that, "at the present stage of international trade [1955], multilateralism and non-discrimination are necessary for the continued development of world commerce" (van Brabant 12). This declaration is exactly opposite to their previous stance on multilateralism, which had precluded them from participation

in the world-wide economic order since 1946.

Guided by their newfound acceptance of multilateralism and a desire to increase trade with the West, the Soviets appealed to the United Nations Economic and Social Council (ECOSOC) for ratification of the Havana Charter and creation of the ITO (Kostecki 8). The Soviet's desire to resurrect the ITO, instead of attempting to join the GATT, stemmed from a combination of factors. First, provisions within the ITO Charter, and not included in the GATT, facilitate the assimilation of NMEs into the international trade sphere. Second, even though East-West relations had thawed, there remained an underlying mistrust. The ITO calmed the fears of the Soviet Union that the U.S. would dominate the forum because the ITO was expected to be based on universal membership (due to the inclusion of technical means for accession to both market economies and NME's) and would be conceived as a United Nations organization (ibid, van Brabant 12) -- where the U.S. and U.S.S.R could begin negotiations on more equal footing. Third, at that time, the Soviet Union ranked relatively low among the trading countries and the GATT did not provide an appropriate framework for establishing Soviet influence in the international trading system. (Kostecki 13). While the Soviet initiative to reestablish the ITO represented a significant ideological turn-about, it was met with distrust and was refused by Western governments who considered the Havana Charter (ITO) a dead letter.

Nine years later, in 1964, the Soviet Union submitted a draft resolution to create a new ITO under the auspices of the United Nations (Sokil 271). This resolution, much like the original ITO and the Soviet proposal of 1955, tolerated the S.U.'s state monopoly

of foreign trade and payments and offered technical arrangements to help reconcile a trade monopoly with the goals of trade expansion based on reciprocity (Sokol 277).

According to the proposal, the technical arrangements necessary to facilitate state trading with market economies would be based primarily on a purchase agreement where non-market economies promise to purchase at least some minimum negotiated value of goods from other members in exchange for tariff reductions by the market economies. The tasks of the proposed organization would include the elimination of "artificially created restrictions and obstacles to trade" and of the "adverse effects of the activities of closed economic groupings on the trade of third countries" (ibid).

Once again, the Soviet Union had reversed itself. Multilateralism and non-discrimination had once again become an acceptable means to increase trade by lowering barriers. The change in the Soviet Union during this time, however, was overshadowed by advances in the rest of Eastern Europe. Not only did these countries accept multilateralism, they asked for, and gained, admittance into that bastion of Western trade control--the GATT.

In the mid-1950's, East-West trade experienced a high rate of growth; it grew faster than trade overall, within CMEA, and even among the industrialized nations (Kostecki 10). This growth of commercial relations necessitated a traders forum to settle differences on commercial matters otherwise lacking in the East-West sphere. After the Soviet failure to resurrect the ITO, Eastern Europe turned to the GATT.

From the Eastern bloc's point of view, the GATT not only presented the opportunity to be a member of a traders forum, but also gave them a chance to decrease

Western discrimination against their exports and an opportunity to compensate, at least partially, for market losses sustained by some CPE's due to the creation and subsequent enlargements of the European Community (Kostecki 13). The detente experienced during the 1950's, and the subsequent accession of Eastern European CPE's into the GATT, was due in part to a significant change in the Western view of the East. The West saw the changes (openings) within the Eastern bloc as an opportunity to both increase trade with CPE's and facilitate its foreign policy objectives.

The West expected the participation of Eastern European countries in the GATT to bring commercial advantages by providing a framework for negotiating reciprocity agreements, assuring new market openings for Western products, and finding a solution for the problem of non-discrimination both in East-West trade and in the context of CMEA commercial relations. Accession of Eastern European countries to the GATT would also provide a unique opportunity for agreement on codes of conduct in commercial matters, especially on issues such as dumping, market disruption, and the exchange of information on trade. This economic viewpoint acquired particular importance from the mid-1960's on as American GATT supremacy was challenged by the emergence of a strong Western Europe (Kostecki 16).

According to the Western view, inclusion of the East in the GATT would not only better its economy, but would also become an instrument for the modification of centrally planned systems and a means of helping those countries increase their independence within the Eastern bloc. This new "ostpolitik" followed three principles. First, a theory of gradualism, which holds that a

sudden transformation of CPE's into liberal societies is impossible, was implemented. Second, the West stopped thinking of Eastern Europe as one bloc. Third, it became conceivable that the West might stop judging the Eastern European economies according to its own liberal philosophy and accept state trading, target control, and central price formation as alternative forms of economic organization (Kostecki 15).

The acceptance of Eastern European countries into market oriented organizations such as the GATT, however, has not been easily accomplished. Even given the Eastern acceptance of multilateralism, non-discrimination, and transparency, the problem of tariffs remained. The concessions enabling CPE's to circumvent the requirement of tariffs have been negotiated in a country by country approach⁵ with no set guidelines or methods. Therefore, investigation of these methods has required a case-by-case analysis of the four Eastern European countries--Poland, Romania, Hungary, and Yugoslavia (Bulgaria received observer status in 1967, but has not made any progress toward full membership and Czechoslovakia was already a member of GATT when a Soviet coup changed its economy to central planning)--which have successfully acceded to the GATT.

YUGOSLAVIA

Observer 1950, Associate Member 1959, Member 1966

Yugoslavia is a good example of how a CPE, given sufficient political will, can join the GATT unconditionally. In the nine years after receiving GATT observer status, Yugoslavia took significant steps to decentralize its economy. These changes were rewarded by acceptance into the GATT as an associate member, which meant that trade relations with other GATT members would be conducted to the extent possible given

Yugoslavia's economic system. While not full accession, this agreement showed that the GATT members believed that movement toward a decentralized economy was possible. Buoyed by this decision, Yugoslavia decentralized its economy, introduced tariffs, abolished multiple exchange rates, and became multilateralist in its trade relations. The introduction of meaningful tariffs was difficult, however, because of price disparities between Yugoslavia and the rest of the world. This problem was overcome and, after further decentralization of its economy, Yugoslavia obtained full GATT membership in 1966 under the normal GATT obligations as exists among other contracting parties (Kennedy 30).

POLAND

Observer 1957, Associate Member 1959, Full Member 1967

After witnessing Yugoslavia's success within the framework of GATT, Poland decided to make an attempt at accession. At first they initiated Yugoslavian style market reforms, but after these reforms failed, Poland proposed acceptance into the GATT based solely on global import commitments. This proposal was approved and after being granted associate status, Poland and the GATT contracting parties agreed to a specific schedule where Poland was required to "increase the total value of its imports from the territories of contracting parties by not less than seven per cent per annum" (Kennedy 31). This formula was based on reciprocity--in exchange for Poland's commitment, the GATT contracting parties would make tariff concessions on Polish imports (Kostecki chapter 4).

ROMANIA

Observer 1957, Full Member 1971

Romania's chronic balance of payments problem caused them to reject outright any measure of import performance that was not tied to its export performance with GATT contracting parties. Consequently, in its protocol of accession, Romania stated that it "firmly 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 for in its five year plan" (Kennedy 32). Unlike the Polish case, Romania's undertaking does not refer to any specific rate of annual import increase (Kostecki chapter 4).

HUNGARY

Observer 1966, Full Member 1973

Even though Poland and Romania preceded Hungary into the GATT, the Hungarian government did not follow their paths to accession. Instead, it followed the Yugoslav pattern and sought GATT membership solely on the basis of tariff concessions. At first, GATT members were understandably concerned that Hungary's state monopoly on trade would subvert the market and make meaningful tariff reductions impossible. However, following the decentralization of its economy in 1968, Hungary convinced GATT members that the Hungarian economy could operate within the framework of the GATT. It was then accepted as a full member on the basis of tariff concessions, but with a commitment to reduce relatively high tariffs (Kennedy 33, Kostecki chapter 4).

Even though these four cases are varied in circumstance and GATT members decided how a given CPE can be admitted through case-by-case analysis, two patterns have emerged. First, in the Polish and Romanian cases, full GATT membership was granted without a change of their CPE or trading system. Instead, the GATT members

decided to follow the method prescribed in the American Suggested ITO charter (and the Soviet suggested charter of 1955 and 1964) which accepts state trading, but requires certain numerical import concessions. On the other hand, Yugoslavia and Hungary were admitted only after showing that their economies were market oriented and that any tariff concession would be meaningful. In order to do this, Yugoslavia and Hungary made massive changes within their economic structures.

Yet, despite these successes, problems persist. Eastern Europe still suffers a massive balance of payments problem caused by their exports not growing sufficiently (a problem they attribute to Western negligence and ascribed by Westerners to the non-convertability of Eastern currency and poor product quality) to finance the level of import spending they agreed upon to enter the GATT. From the Western point of view, the Polish and Romanian commitments to increase imports have not successfully lowered trade barriers (Kennedy 36).

In searching these two models for a way whereby the Soviet Union could enter the GATT, one encounters problems. The terms of acceptance used by Poland and Romania have been criticized by GATT members as ineffective. Additionally, the Soviet Union, alleging that a conditional relationship would result in second-class treatment, has refused (beginning in the late 1960's) to join the GATT under these conditions (Kostecki 14). That leaves the Hungarian/Yugoslavian model. Under these requirements, the Soviet Union would need to make massive market-oriented and decentralizing changes in its economy.

Unless the Soviet Union is willing to make these changes (barring the creation of

a new method of accession by the GATT members), the granting of full GATT membership to the Soviets is unlikely. However, under General Secretary Mikhail Gorbachev, some of these reforms have been implemented. It is the existence of these reforms that have once again opened the avenue of GATT acceptance to the Soviet Union.

**SOVIET ACCEPTANCE
OF
INTERNATIONAL ECONOMIC INSTITUTIONS
(1986-PRESENT)**

Since General Secretary Gorbachev came to power in 1985, the world has discovered a changing Soviet government. Glasnost and perestroika have become household words and economic reform in the Soviet Union is widely discussed among people throughout the world. This "restructuring" has also affected the Soviet's attitude toward the GATT (Gardner 7). According to Gorbachev, the Stalinist autarkic economic system has outlived its usefulness. While granting that totalitarian planning may have hastened Soviet industrialization in the 1930's and mobilization in the 1940's, Gorbachev feels that it is no longer applicable in today's world of interdependence and rapid technological change (Sokil 380).

Ever since the detente of the mid-50's, the Soviets have been increasing their level of foreign trade. However, it is just recently that they have begun to trade in significant numbers as compared to the rest of the world. In the last twenty years, Soviet trade has increased so much that they are now the sixth largest exporter of merchandise trade and seventh in imports of merchandise trade. In 1988, 39 per cent of the Soviet Union's exports of merchandise trade was destined for the West (Kennedy 24).

Even though Moscow acknowledged the legitimacy of a multilateral system of trade negotiations in 1955, it was not ready to accept the GATT as the document governing trade relations--shown by their desire to ratify the ITO Charter instead of

seeking membership in the GATT. While many problems precluded this from happening, one of the biggest was the fear of US dominating within the forum. Now, however, with the Soviet's growing economy and the emergence of a strong Europe and Pacific Rim, Moscow believes that U.S. power, while still strong, is not dominant. Additionally, despite repeated requests from the Soviet Union for ratification of the ITO Charter, no action was taken. This left the Soviets with no other multilateral outlet for trade negotiating with Western governments. Once again, GATT became the accepted power by default.

Due to the changes addressed above and needs that will be discussed later, the Soviets formally applied for GATT participation during the eighth and last round of GATT talks on 15 August 1986. The Soviets requested observer status, with full membership in the GATT to follow in due course. However, this request was rejected (Kennedy 23).

While the political changes within the Soviet Union enabled Moscow to make the application, the driving forces behind the request are economical and can be divided into three parts: a need to increase trade knowledge and familiarity, a desire for accession into an international traders forum, and a need to increase revenue from foreign trade.

INCREASED FAMILIARITY

In the past, trade with the Soviets occurred at a low level and was dominated by Foreign Trade Organizations (FTO's). Due to this intervention, few of today's Soviet managers and enterprise leaders know how to operate within a multi-national sphere (Gardner 9). However, as part of Gorbachev's "restructuring", some enterprises have

been given the freedom to circumvent the FTO's and conduct trade on their own. This necessitates a need for many more trade experts. The Soviet Union is hoping to use the GATT to increase Soviet familiarity with trade (Eklof 91) by observing other GATT member's practices and increasing their own trade levels.

TRADERS FORUM

The Soviet Union, much like the Eastern Europe of the late 1950's, wishes to be involved in an international trade body in order to get its voice heard and reduce trade restrictions regarding exports (Kostecki 42). From the Soviet point of view, given the present increase of both Soviet trade (Moscow now trades with 145 different countries) and GATT coverage (91 countries and 4/5 of world trade (Morrison 5)), it "is reasonable that it should wish to take part in the international bodies governing [trade]" (Aganbegyan 154). Additionally, the Soviet Union is the only CPE with no affiliation with the GATT (Sokil 308) and it has had thirty years to observe the advantages granted other NME's from GATT participation.

INCREASE TRADE REVENUE

The Soviets, and most Western analysts, believe that acceptance into the GATT will reduce Western trade barriers (Hewett 380) by assuring the Soviets MFN status and an opportunity to give and receive trade concessions. Even though the U.S. is the only major Western nation that has not granted MFN status to the Soviet Union⁶ (Holzman 29), the granting of universal MFN status would help the Soviets achieve a desired shift of exports from primary products to manufactured goods (Sokil 380).

Gorbachev needs gains from trade, which would accelerate after GATT

acceptance, for two things: to give economic support to perestroika (Eklof 90) and to help fulfill the massive expansion to be accomplished during the five-year plan that began in 1986 (Gardner 7). The restructuring of the economy, as planned by perestroika, requires massive amounts of capital to smooth the way for market, and especially price, reforms (Zarocostas 1). The easiest method to gain this is through a combination of loans and gains from trade, both of which would be easier after the normalization of trade relations which would occur following accession to the GATT. Furthermore, the free market requirements of the GATT would give more room to newly autonomous enterprises to maneuver and engage in trade. "Participation in the GATT and economic reform are reinforcers that build on each other" (van Brabant 4).

Following the Party conference in 1986, it was announced that during the 12th five-year plan period (1986-1990) more than one-third of all Soviet productive assets are scheduled for modernization or replacement (Gardner 6). At this same time, both the international demand for oil and oil prices fell. Because oil serves as the Soviet's largest export, this decrease in oil revenue magnified Soviet concerns that they would have difficulty financing the imports necessary to meet the five year plan (Sokil 380, Gardner 6, van Brabant 4). Gorbachev is therefore hoping to use revenue gained from other exports and gains from trade to make up the loss of oil revenue. Both of these goals would be greatly facilitated by acceptance into the GATT.

However, Moscow's acceptance to the GATT, due to both technical problems and a skewed Western perception of the Soviets, is going to be a long, laborious, and perhaps impossible task. The problems facing the Soviets are much like those that faced Poland,

Hungary, Romania, and Yugoslavia before their accession to the GATT, but magnified many times because of the Soviet economy's larger size.

The GATT, in its traditional form and usage, was drafted for market economies and controlled trade by means of a tariff system. However, CPE's control their trade by plan targets. This discrepancy leads to a difficulty in applying GATT provisions to state-trading economies that is exacerbated by the enormous size of the Soviet economy. Requirements to enter the GATT, as discussed previously, are divided into four major areas: non-discrimination, reciprocity, transparency, and tariffs. Each of these requirements is accompanied by problems unique to CPE's and the Soviet Union

NON-DISCRIMINATION

The GATT, per article XVII, imposes a "commercial considerations only" clause on the conduct of state trading enterprises. However, this runs contrary to past Soviet practice⁷. As Lenin explained, "everything pertaining to commerce is a matter of public law and thus serves a public, and hence a political, function" (Kennedy 34).

In order to assure that political considerations would be taken into account in dealing with economic decisions, NME's long ago turned to a system of Central Planning. Under this system, an irrational pricing structure (where the cost of production is not linked to the consumer's cost) and a governmental monopoly of trade (which leads to no links between foreign and domestic prices) has emerged. Because of the lack of "real prices", the GATT's goal of promoting and assuring non-discrimination in trade is difficult to achieve (Hewett 29, Kostecki 35).

Yet, once a country has agreed to practice non-discrimination, there are several

means of assurance, even under direct trade control. This may be accomplished "on the basis of traders previous shares, respective production capacities of exporting countries, or on a first come first served basis" (Kostecki 52).

RECIPROCITY

Another issue arising out of the difficulty of determining a "real" price in a CPE is the identifiability of tariffs. Without the ability to determine a tariff level, it is very difficult to insure that reciprocity will occur. In the past, trade negotiations were conducted on a tariff reduction for tariff reduction basis. However, with the introduction of NME's to the GATT, negotiations between a market economy and an NME have occurred on an asymmetric basis where a tariff reduction is granted in return for another type of trade barrier reduction. This type of formula, while possible, further complicates the negotiation process by "adding to the already difficult task of calculating the balance of costs and benefits of equivalence between various instruments of concession making (tariffs, quotas, import targets, licence, and subsidies)" (Kostecki 40).

There are two established methods for an NME, such as the Soviet Union, to fulfill the requirement of reciprocity and they have already been addressed within this paper.

TRANSPARENCY

The issue of transparency is a perplexing. While this is arguably the groundwork upon which all negotiations are made (Sokil 278), it is also the most difficult to obtain from NME's. In addition to the problems listed above (assurance of reciprocity and non-discrimination), the application of anti-dumping laws to NME's requires a high degree

of knowledge concerning domestic price and cost structures (Kennedy 37).

Even though this problem appears overwhelming, it can be solved without special technical arrangements. If the Soviet Union will agree to periodic consultations, inspections, and an open book policy (like Hungary and Romania did), then transparency would not be as large a problem. However, even with glasnost, it may be difficult to ensure that the appropriate data will be given.

TARIFFS

The GATT requires (with certain exceptions like Poland and Romania) that a country control trade by tariffs only and not by quantitative restrictions. This is difficult to accomplish and enforce in an NME (Sokol 281) because no links exist between foreign and domestic prices. Therefore, in order for the Soviet Union to gain acceptance into the GATT (because they have already rejected acceding to the GATT by methods similar to Poland's and Yugoslavia's), Moscow must institute a meaningful set of tariffs. Judging from the case history of Yugoslavia and Hungary, this will be a long and difficult process.

Non-discrimination, reciprocity, transparency, and tariffs are all ideals that stand between the Soviet Union and its goal of full participation in the GATT. However, guided by Gorbachev, the Soviet Union is now making the changes necessary to meet these GATT requirements (van Brabant 3).

Gorbachev's rise to power has facilitated the change of many institutions within the Soviet system: the State's planning power has decreased, export producers have been

given the right to retain foreign currency, and prices have become more representative of costs. All of these changes help move the U.S.S.R. toward the creation of a market influenced economy, and additionally towards the GATT.

The Stalinist trade system was established so that the Soviet Union's State Planning Commission and the Ministry of Foreign Trade determined the level and composition of foreign trade. The most influential trade organ within these agencies was the Foreign Trade Organizations (FTO). By guiding all trade requests through these organizations, Moscow insured that non-economic considerations would be applied to the decision making process and that market forces would have a minimum affect (Kennedy 34). While this policy did achieve governmental goals of control, it also decreased trade levels.

Therefore, in order to increase the amount of foreign trade, the Soviet government has begun to liberalize its trade monopoly and give a higher degree of autonomy to individual enterprises. In February 1986, the Supreme Soviet passed an act authorizing 21 national agencies and 68 large enterprises to handle their own foreign transactions. While not large in number, the liberalized organizations constituted 20% of total Soviet trade and 60% of machinery exports. One year later, in 1987, the Ministry of Light Industry and 8 other industrial enterprises were also given the right to trade directly with foreign buyers (Gardner 9, Eklof 91).

The state's previous monopoly on trade was also decreased by bureaucratic reforms. The Ministry of Foreign Affairs was downsized from eight major administrators to four and in 1988 the Ministry of Foreign Trade was combined with the

State Committee for Foreign Relations. The downsizing of these groups led to a decrease in staff, and thus, of influence.

These reforms increased the autonomy of some enterprises and ministries within the Soviet Union and gave them free reign over trade decisions. However, there still remains many obstacles to be overcome before trade will markedly increase.

The next major reform called for a change in the Stalinist method of paying export producers. Until 1987, exporters were paid with domestic currency and all foreign monies earned were taken by the state. While this practice allowed the government to maintain control over the volume and composition of imports (because foreign currency is needed to buy any Western import), it provided little incentive for export production.

The Foreign Trade Reform Decree changed this practice. Now, enterprises are allowed to keep foreign exchange monies in accounts which are inviolable, easy to use, and not subject to FTO scrutiny. This decision was reinforced by the 1987 Supplemental Decree which declared that enterprises may decide how to spend their money and that their purchases should (for those enterprises not authorized to conduct foreign trade on their own) be given highest priority by the FTO's (Gardner 10, Goldman 80,).

Another problem in the way of Moscow's achieving an increased level of trade and acceptance into the GATT is the Stalinist pricing system. Under this system, industrial wholesale prices were set so that most enterprises could cover their costs. But several goods, especially basic foodstuffs and transportation, were priced so low that they had to be subsidized from the state budget. Gorbachev, in hopes of eliminating the

excess taxes and subsidies distorting the economy's operation, plans on introducing a system of prices that reflect production costs (Gardner 9). This reform, however, is highly controversial within the Soviet Union (a country where government subsidized low prices have become the norm) and will undermine Gorbachev's popular support.

While these and other market oriented changes were initiated to improve the economic standing of the Soviet Union as a whole, they also serve as legitimate evidence that Moscow is serious about making the market oriented reforms necessary to join GATT. Yet, the final judge of Soviet intent is not Moscow, but rather the West and, apparently, they are not convinced.

The Soviet's initial request for GATT observer status was summarily refused (at the instigation of the U.S. (van Brabant 6)) on the basis of Moscow's non-market orientation (Kennedy 23). Once again in 1989, following a constant Soviet push for observer status and the instigation of many market oriented reforms, the West still would not approve the granting of observer status to the Soviets--due ostensibly to the Soviet failure to make sufficient progress in instituting a free-market economy (Cooper 674).

Western forecasts regarding the future of Soviet/GATT relations also key on the changes necessary for Soviet assimilation into the GATT (Kennedy 28, 35). Most analysts feel that if Gorbachev is successful in his reforms, then the Soviets could successfully turn to the GATT to decrease trade barriers (Hewett 384). On the other hand, if his reforms go poorly, the opposite will result.

There is ample evidence that the Soviets are legitimately attempting to change their economy and become a "team player" with the West. However, the U.S. and other

nations have been very slow to recognize this. The Soviets have made market reforms similar to those instituted in Yugoslavia before it was granted observer status, yet, the Soviet appeal was denied. Why? Cold War politics.

With Soviet accession to the GATT doing no harm to member countries and providing the Soviets with useful insights concerning the implementation of their domestic reform policies and the changes necessary to take full advantage of the world trading system (The Institute for East - West Security Studies Working Group on International Economic Change, Restructuring, and East-West Security as quoted in Cooper 677) why else, but politics, would the Soviet request be denied. Granted, a lengthy period of observation is in order to ensure the entrenchment of market oriented reforms and to make any adjustments necessary to Soviet trading practices (it took Yugoslavia sixteen years before gaining full membership), but there is no real excuse for precluding the Soviets from the trade forum.

However, a change of political attitude is in the air. In April 1990, the Bush administration dropped its opposition to Soviet accession. U.S. Trade Representative, Carla Hills, said, "we would not object to observer status if [the Soviets] wanted to come in prior to the end of the round, provided there are no objections from other GATT members (Zarocostas 1).

It is now time to recruit the Soviets into the international economic order. This will finally meet the original goals of a truly international and universal forum for trade discussion.

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FOOTNOTES

1. The State Department, after the Soviet refusal to sign the Bretton Woods draft agreement, felt that the Soviets had fully intended to join as evidenced by a dramatic last-minute acceptance of an increased IBRD quota (Department of State 1388 1946).

2. On 12 April 1944, Molotov told the American Ambassador that "participation in the work [creating the post-war economic institutions] is for the sake of maintaining the appearance of tripartite collaboration" (Department of State 1388). The state department, however, did not take this comment seriously because at this same time the Soviets were actively participating in the discussions. But, this comment does lead one to wonder what Stalin had planned (if even he knew at that time).

3. Following President Roosevelt's death in April 1945, Harry Truman, the new U.S. President, denied lend-lease aid to the Soviets. This could have easily been a signal to the Soviets that post war relations would not be as amenable as they had been.

4. The Soviets, even though invited, absented themselves claiming that they lacked the time to sufficiently study the Western proposals under discussion (Kostecki 2).

5. In deciding how to accept CPE's into the GATT, there were two options: one could introduce into the GATT some general provisions on target-controlled state trading along the lines of the American Suggested Charter or one could use a country by country approach, working out arrangements for particular state trading systems in the GATT. The West decided to use the country by country approach because of its ability to influence these countries politically. Through this, the GATT members hoped to influence the CPE's into decentralization, diversification of commercial policy, and decreasing Soviet power within the bloc (Kostecki 138).

6. The American Jackson-Vanick law which ties MFN status to Jewish immigration policies precludes the Soviets from receiving MFN status.

7. In the process of considering an import license application, the Ministry of Foreign Trade considers whether the product is in the import plan, whether it conforms to a trade agreement with the country in question, the status of the trade balance with that country, and the state of political considerations with that country (Hewett 32).