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LOOKING TO FILL AN INTERNATIONAL REGULATORY GAP: BRAZIL BRINGS THE ISSUE OF EXCHANGE RATES AND TRADE BEFORE THE WORLD TRADE ORGANIZATION

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INTRODUCTION

Concern over the relationship between exchange rates and trade has a long history in both international law and economics. This concern has manifested itself in two primary ways: first, as a worry about the impact of currency fluctuation on trade flows and, second, as a worry about the impact of currency manipulation on fairness in the international trading regime. While there is no consensus on how to address the problems created by the relationship of exchange rates and trade, this lack of consensus has done nothing to diminish states' concerns over the impact of currency fluctuation and manipulation on trade. Rather, increased fluctuation and increased protectionism during the global economic crisis that began in 2008 has led to rising concerns about the impact of exchange rates on trade.¹

In this climate, Brazil recently called for a debate on exchange rates and trade within the World Trade Organization (“WTO”), specifically in the Working Group on Trade, Debt and Finance (“WGTDF”), “with a view to better understanding the issues involved and their implications for members of the WTO.”² Thus far, the Brazilian proposal has led to a review of the academic literature on the relationship of currency fluctuation to trade flows and a two-day meeting in March 2012 to discuss the literature review.³ More

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The views expressed in this article are solely those of the authors and do not reflect the views of the Court of International Trade or any judge on that court.

¹ Working Group on Trade, Debt and Finance, *The Relationship Between Exchange Rates and International Trade: Submission by Brazil*, at 1, WT/WGTDF/W/53 (Apr. 13, 2011) [hereinafter *Brazil Proposal*] (submission by Brazil to the World Trade Organization’s Working Group on Trade, Debt and Finance).

² *Id.* at 1–2.

³ See *infra* notes 68–76 and accompanying text.

recently, Brazil has indicated that it would like to see the discussion move in the direction of possible trade remedies.⁴ The Brazilian proposal raises important questions about the reigning structure of international financial regulation and the future of currency market regulation.

This Recent Development will provide background on Brazil's proposal and identify important issues and possible implications of this proposal for the current structures of international economic regulation, particularly in the context of international trade.⁵

I. BACKGROUND: CURRENCY AND THE WTO FRAMEWORK

The international community has long recognized a link between trade and currency. One aspect of this relationship is a long-held presumption that exchange rate volatility has a negative impact on trade flows.⁶ While current literature on exchange rate volatility and trade flows does not necessarily bear out this conclusion,⁷ such a presumption seemed logical in the aftermath of the Great Depression—a period that witnessed both massive volatility in currency markets and extreme protectionism. The apparent link between exchange rate volatility and trade protectionism during the Great Depression was an aspect of what motivated international leaders to create a new, post-war framework for international economic cooperation and regulation that included the International Monetary Fund (“IMF”) and the General Agreement on Tariffs and Trade (“GATT”). Though the history of these institutions has been treated extensively,⁸ a brief review of their origins and goals provides context for the renewed discussion on exchange rates and trade initiated by Brazil.

⁴ See Working Group on Trade, Debt and Finance, *The Relationship Between Exchange Rates and International Trade: Exchange-Rate Misalignment and Trade Remedies: A Conceptual Note by Brazil*, at 8–9, WT/WGTDF/W/68 (Nov. 5, 2012) [hereinafter Brazil Note] (conceptual note written by Brazil for the benefit of the World Trade Organization's Working Group on Trade, Debt and Finance).

⁵ Neither of the authors is a trained economist, and for this reason we do not attempt to assess the economic arguments that are an essential aspect of this discussion. Rather, our goal is to make the reader aware of this discussion in the arena of international trade law and to suggest, in a broad way, where such a discussion may lead.

⁶ PETER B. CLARK ET AL., A NEW LOOK AT EXCHANGE RATE VOLATILITY AND TRADE FLOWS 1–2 (2004).

⁷ *Id.*

⁸ See, e.g., GOVERNING GLOBALIZATION (Deepak Nayyar ed., 2002); Marc Auboin, *Fulfilling the Marrakesh Mandate on Coherence: Ten Years of Cooperation between the WTO, IMF and World Bank 1* (WTO Discussion Paper No. 13, 2007).

While the Great Depression had a variety of catalysts, historians generally agree that the economic devastation was worsened by the competitive devaluation of major currencies⁹ and the implementation of trade barriers to protect domestic economies.¹⁰ As consumer buying power declined and trade diminished, global export production fell, resulting in widespread unemployment and poverty.¹¹ The international community responded to the Great Depression, in part, by addressing the devastating lack of cooperation among countries in the face of crisis through a set of institutions and policies that came to be known, collectively, as the Bretton Woods System.¹²

Named for the Bretton Woods Conference of 1944, where it was developed, the elements of the Bretton Woods System remain the foundation for the current architecture of international economic regulation. A tripartite set of institutions responsible for international economic regulation was proposed at Bretton Woods: the IMF, the World Bank Group (“World Bank”),¹³ and the International Trade Organization (“ITO”).¹⁴ The IMF and World Bank were quickly approved.¹⁵ The World Bank was created to provide capital to underdeveloped nations, while the IMF was to lend reserve currencies to nations with a trade deficit and monitor exchange rates.¹⁶ The ITO, which was intended to bring stability to the international trade regime, failed to gain approval.¹⁷ Despite the ITO’s failure, the GATT,¹⁸ drafted during the meeting, was given provisional effect; however, instead of being administered by the ITO, a small staff in Geneva was given the task until 1995 when the GATT fell under the auspices of the WTO.¹⁹

⁹ E.g., Charles Blum, *Foreword: The Question of Currency Manipulation*, 10 J. INT’L BUS. & L. 207, 207 (2011); see also, e.g., *Cooperation and Reconstruction (1944–71)*, INTERNATIONAL MONETARY FUND, <http://www.imf.org/external/about/histcoop.htm> (last visited Jan. 22, 2013).

¹⁰ E.g., Auboin, *supra* note 8, at 4.

¹¹ *Id.*

¹² Jeffrey S. Beckington & Matthew R. Amon, *Competitive Currency Depreciation: The Need for a More Effective International Legal Regime*, 10 J. INT’L BUS. & L. 209, 209 (2011).

¹³ The World Bank Group was originally known as the International Bank of Reconstruction and Development. *Id.* at 211.

¹⁴ *Id.*

¹⁵ See *id.* (stating that the IMF and World Bank were established at the Bretton Woods Conference itself).

¹⁶ Jong-Il You, *The Bretton Woods Institutions: Evolution, Reform, and Change*, in GOVERNING GLOBALIZATION, *supra* note 8, at 209, 210–11.

¹⁷ Beckington & Amon, *supra* note 12, at 220–22.

¹⁸ General Agreement on Tariffs and Trade, Oct. 30 1947, 61 Stat. A-11, 55 U.N.T.S. 194 [hereinafter GATT].

¹⁹ Beckington & Amon, *supra* note 12, at 220–22.

A critical, non-institutional element of the Bretton Woods System was a new exchange rate regime to replace the gold standard. The gold standard had failed to maintain exchange rate stability during the inter-war period, and the representatives at the Bretton Woods Conference viewed currency stability as essential to rebuilding the global economy.²⁰ Under this new regime, countries agreed to fix their exchange rates to the U.S. dollar, while the U.S. dollar was linked to gold in order to have exchangeable currencies at stable and predictable rates.²¹

Concern over the impact of exchange rate volatility included concern over its effect on trade, and delegates raised this issue in the context of the ITO negotiations. Specifically, during the Havana Charter negotiations, parties recognized that “devalued currencies might constitute a form of unfair trade,” and the Australian delegation put forward a proposal to include “currency dumping” as a remediable trade practice.²² The Australian proposal was dismissed during the negotiations, and concerns over currency fluctuation were not ultimately addressed as remediable practices in the GATT.²³ Evidence of the concern over the effect of exchange rate volatility on trade is not, however, entirely absent from the GATT; rather, as discussed below, several GATT articles address various aspects of the relationship between exchange rates and trade, but none create a trade remedy for imbalances occasioned by exchange rate fluctuation.²⁴

The Bretton Woods’s fixed exchange rate system ended in 1971 when U.S. President Richard Nixon severed the link between the value of the U.S. dollar and the value of gold.²⁵ Once the United States delinked the dollar from gold, other major economies around the world stopped fixing their currencies to the

²⁰ R.S. GORSKI, SUMMARY REPORT ON BRETTON WOODS MONETARY CONFERENCE 1–2 (1945), available at http://fraser.stlouisfed.org/docs/historical/martin/18_03_194505xx.pdf.

²¹ MICHAEL W. KLEIN & JAY C. SHAMBAUGH, EXCHANGE RATE REGIMES IN THE MODERN ERA 27 (2010); see Beckington & Amon, *supra* note 12, at 237.

²² See United Nations Conference on Trade and Employment, Lake Success, N.Y., Jan. 20–Feb. 25, 1947, *Report of the Drafting Committee of the Preparatory Committee*, at 13, U.N. Doc. E/PC/T/34 (Mar. 5, 1947); see also Brazil Note, *supra* note 4, at 2 (discussing Australia’s proposal to regulate the use of “currency dumping duties”).

²³ Brazil Note, *supra* note 4, at 2.

²⁴ See GATT, *supra* note 18, art. II:6 (permitting specific tariff adjustments to counteract the effect of currency devaluation); *id.*, art. XV:4 (prohibiting frustration of the GATT through exchange action or frustration of the Articles of Agreement of the International Monetary Fund through trade action); see also Brazil Note, *supra* note 4, at 2. These GATT articles are discussed further *infra* Part III.

²⁵ JONATHAN E. SANFORD, CONG. RESEARCH SERV., RS22658, CURRENCY MANIPULATION: THE IMF AND WTO 1 (2011).

dollar and, instead, let their exchange rates float.²⁶ Following the end of the Bretton Woods fixed exchange rate system, the international community did not create a replacement mechanism to provide what WTO Director General, Pascal Lamy, has referred to as a “sense of organized governance in the international monetary system.”²⁷ Rather, in the post-Bretton Woods world, a variety of exchange rate regimes exist: Some states allow exchange rates to float freely (what is sometimes referred to as market-determined rates); some states allow rates to float within a range of values; and others continue to peg their currency’s value to a foreign currency.²⁸

The end of the Bretton Woods fixed exchange rate system meant two things for the international monetary system. First, as discussed above, exchange rates are largely unregulated. The IMF plays an advisory role, with the goal of stabilizing exchange rate policy, but it does not have any direct regulatory authority over exchange rate regimes.²⁹ Second, the end of Bretton Woods’ fixed exchange rates meant that individual countries could directly affect their own exchange rates, and the possibility of currency manipulation became an important focus of international concern.³⁰ The basic formulation of this concern is as follows: If an exporting country intervenes to keep the value of its currency low, such devaluation drives down the price of exports from that country allowing its exporters to undercut both the domestic industry in an importing country and other competing foreign exporters.³¹ Recent attention paid towards the issue of currency manipulation has largely focused on accusations of currency manipulation by the United States against China.³² China has historically intervened in exchange markets to, in China’s view, maintain the stability of its currency.³³ However, many policymakers and

²⁶ See You, *supra* note 16, at 211–12.

²⁷ Pascal Lamy, Director-General, Opening Remarks at the WTO Seminar on Exchange Rates and Trade (Mar. 27, 2012) (transcript available at http://www.wto.org/english/news_e/sppl_e/sppl222_e.htm).

²⁸ KLEIN & SHAMBAUGH, *supra* note 21, at 27–28. As Klein and Shambaugh note, this is a simplified categorization, and most countries employ different exchange rate policies at different times or in concert. *Id.* at 29–30.

²⁹ See Sungjoon Cho & Claire R. Kelly, *Promises and Perils of New Global Governance: A Case of the G20*, 12 CHI. J. INT’L L. 491, 528 (2012).

³⁰ SANFORD, *supra* note 25, at 1–2.

³¹ See Bryan C. Mercurio & Celine Sze Ning Leung, *Is China a ‘Currency Manipulator’? The Legitimacy of China’s Exchange Regime Under the Current International Legal Framework*, 43 INT’L LAW. 1257, 1296 (2009).

³² For a discussion of the U.S. approach to Chinese currency intervention, see SANFORD, *supra* note 25, at 4–5.

³³ *Public Announcement of the People’s [sic] Bank of China on Reforming the RMB Exchange Rate Regime*, PEOPLE’S BANK OF CHINA (July 21, 2005), <http://www.pbc.gov.cn/publish/english/955/2001/20014/>

scholars argue that Chinese intervention is intended to keep the value of its currency artificially low and, consequently, more competitive against other foreign currencies.³⁴ In light of the potential impact on trade flows and domestic industry, U.S. lawmakers have repeatedly attempted to pass legislation making Chinese currency practices a countervailable subsidy subject to offset by countervailing duties.³⁵ Though these efforts have not yet been fruitful, they highlight the potential impact of concerns over currency manipulation on the law of international trade. Furthermore, direct intervention to control currency valuation is not the only practice that raises international concerns over currency manipulation. Other states have begun to target accusations of manipulation against the United States for what they perceive as the manipulative effect on currency value that results from U.S. fiscal policy, particularly the Federal Reserve's policy of quantitative easing.³⁶ It is this broader notion of manipulative currency practices that Brazil is targeting with its efforts to remedy what it refers to as "currency misalignment."³⁷

This is the context in which Brazil first proposed a program of study and discussion in the WGTDF, and more recently suggested that the discussion be taken in the direction of trade remedies. Before addressing Brazil's proposal, however, it is worth asking whether, under the current regime of international trade law, the WTO or its member states have the tools to fill this regulatory gap.

II. THE CURRENT INTERNATIONAL TRADE REGIME AND EXCHANGE RATES

When looking for current responses available to the WTO and its member states, the GATT is the logical first place to look. Not surprisingly, Brazil

20014_.html [hereinafter *Public Announcement*] ("The People's Bank of China is responsible for maintaining the RMB exchange rate basically stable at an adaptive and equilibrium level, so as to promote the basic equilibrium of the balance of payments and safeguard macroeconomic and financial stability.").

³⁴ See, e.g., C. Fred Bergsten, *The Need for a Robust Response to Chinese Currency Manipulation—Policy Options for the Obama Administration Including Countervailing Currency Interventions*, 10 J. INT'L BUS. & L. 269, 272–73 (2011); Benjamin Blase Caryl, *Is China's Currency Regime a Countervailable Subsidy? A Legal Analysis Under the World Trade Organization's SCM Agreement*, 45 J. WORLD TRADE 187, 187–88 (2011).

³⁵ For examples of American lawmakers' attempts at counteracting China's currency manipulation, see Mercurio & Leung, *supra* note 31, *passim*.

³⁶ See, e.g., *Bernanke Says the Fed's Latest Monetary Policy Could Benefit the Global Economy*, N.Y. TIMES, Oct. 15, 2012, at B2 [hereinafter *Bernanke Defends Fed Policy*]; John Paul Rathbone & Jonathan Wheatley, *Brazil's Finance Chief Attacks U.S. over QE3*, FIN. TIMES, Sept. 20, 2012, <http://www.ft.com/intl/cms/s/0/69c0b800-032c-11e2-a484-00144feabdc0.html>.

³⁷ Brazil Note, *supra* note 4, at 1–2; *accord* Rathbone & Wheatley, *supra* note 36.

addresses the application of the GATT in its most recent submission, identifying three potential but ultimately insufficient articles.

First, Article II:6 permits a country to adjust its scheduled tariffs higher to account for devaluations in its currency, thereby maintaining the effectiveness of the tariff rate, so that the country does not lose benefits it negotiated for in its WTO accession talks or subsequent negotiations.³⁸ This tool, however, is limited to protecting effective tariff rates due to a country's own currency depreciation and cannot be used in instances of currency appreciation, nor can it be used by a country threatened by imports made cheaper by depreciation in an exporting country's currency value.³⁹

Brazil also looks to Articles XV and XXIII, which are intended to provide broader protection to the value of agreed upon concessions.⁴⁰ Pursuant to Article XV:4, countries should not be permitted to frustrate the intent of the GATT through exchange rate practices.⁴¹ Brazil dismisses Article XV:4 as "not designed to equip Contracting Parties with the means to deal with the new challenges created by the weakness of the international monetary system following the collapse of the gold standard, nor to settle any related trade dispute."⁴² As Brazil notes, an exchange rate practice must frustrate both the letter and appreciably depart from the intent of the GATT in order to violate Article XV:4,⁴³ which places a high bar on determining that an action frustrates a provision of the GATT. Article XXIII:1(b) provides even broader protections, allowing a contracting party to challenge the application of any measure by another contracting party that impairs or nullifies any benefit accruing under the GATT, whether or not the measure conflicts with a

³⁸ GATT, *supra* note 18, art. II:6 ("The specific duties and charges . . . and margins of preference in specific duties and charges maintained by such contracting parties, are expressed in the appropriate currency at the par value accepted or provisionally recognized by the Fund at the date of this Agreement. Accordingly, in case this par value is reduced consistently with the Articles of Agreement of the International Monetary Fund by more than twenty per centum, such specific duties and charges and margins of preference may be adjusted to take account of such reduction.").

³⁹ See Brazil Note, *supra* note 4, at 4–5.

⁴⁰ *Id.*

⁴¹ GATT, *supra* note 18, art. XV:4 ("Contracting parties shall not, by exchange action, frustrate the intent of the provisions of this Agreement, nor, by trade action, the intent of the provisions of the Articles of Agreement of the International Monetary Fund.").

⁴² Brazil Note, *supra* note 4, at 5.

⁴³ GATT, *supra* note 18, Annex I (noting in the supplementary notes to Article XV:4 that "[t]he word 'frustrate' is intended to indicate, for example, that infringements of the letter of any Article of this Agreement by exchange action shall not be regarded as a violation of that Article if, in practice, there is no appreciable departure from the intent of the Article"); Brazil Note, *supra* note 4, at 5.

provision of the GATT.⁴⁴ Brazil also rejects an Article XXIII:1(b) action as requiring too high a burden because the complainant must both provide a “detailed justification” and “is likely to have to demonstrate that the measure adversely affects the competitive position of its products and that it was impossible to predict the adverse competitive position stemming from the measure when the concessions affected by the measure were negotiated.”⁴⁵

In short, Brazil argues that neither Article XV:4 nor XXIII:1(b) was intended to address the situation of currency misalignment and that each places a burden on the complainant that would make it too difficult to show that a practice resulting in currency misalignment either frustrates the intent of the GATT or results in a nullification or impairment of benefits. Brazil is correct that neither provision was drafted in contemplation of addressing exchange rate practices, precisely because they were drafted in a context in which exchange rates were the province of the IMF.⁴⁶ Furthermore, there are high burdens under these actions because they are exceptional, and Brazil is likely correct that it would be quite difficult to bring a complaint against an exchange rate policy under either provision, though it is an untested proposition. In the end, however, these provisions do not appear to provide the efficient and effective response to the adverse trade impact of currency misalignment that Brazil believes is necessary.⁴⁷

⁴⁴ GATT, *supra* note 18, art. XXIII:1(b) (“If any contracting party should consider that any benefit accruing to it directly or indirectly under this Agreement is being nullified or impaired or that the attainment of any objective of the Agreement is being impeded as the result of . . . the application by another contracting party of any measure, whether or not it conflicts with the provisions of this Agreement.”).

⁴⁵ Brazil Note, *supra* note 4, at 5.

⁴⁶ *See, e.g.*, GATT, *supra* note 18, art. XV (making questions or disputes regarding exchange rates and other fiscal policy matters subject to coordination and cooperation with the IMF).

⁴⁷ *See* Brazil Note, *supra* note 4, at 6 (noting in the context of Article II:6 that negotiations could not be expected “to deliver timely solutions for Members in need for immediate relief on account of more or less enduring but disruptive impacts of currency misalignments”). In this regard it is worth noting that Article II:6, Article XV:4, and Article XXIII:1(b) actions must be decided through negotiation or by the WTO before corrective action can be taken. GATT, *supra* note 18, arts. II:6(a) (requiring collective action pursuant to art. XXV), XXII (requiring consultation “with respect to any matter affecting the operation of this Agreement”), XXIII:1–2 (requiring bilateral consultation followed by multilateral consultation and investigation of alleged acts of nullification or impairment). By contrast, with a trade remedy, the importing country can take action upon its own initiative and then the onus is on the exporting country to initiate a challenge before the WTO. *See, e.g.*, Int’l Trade Admin., Dep’t of Commerce, *An Introduction to U.S. Trade Remedies*, <http://ia.ita.doc.gov/intro/index.html> (last visited Feb. 6, 2013) (describing the unilateral process of assessing a trade remedy); *see also* Understanding on Rules and Procedures Governing the Settlement of Disputes apps. 1–2, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 2, 1869 U.N.T.S. 401 [hereinafter DSU] (listing those agreements and provisions of the GATT covered by the DSU).

It has also been suggested that illegitimate currency practices might be corrected under the auspices of current trade remedies: safeguards, antidumping duties, or countervailing duties. The use of countervailing duties is the most likely of these three options.⁴⁸ Whether there is a basis under the current WTO system for making currency manipulation a countervailable subsidy is, however, subject to debate.⁴⁹ The WTO's Agreement on Subsidies and Countervailing Measures ("SCM Agreement") was enacted with the goal of disciplining government interventions that distort international trade or have the potential to do so.⁵⁰ According to the SCM Agreement, a subsidy is a "financial contribution" or "any price support" offered by a government or any public body within the territory of a Member State, which confers a benefit.⁵¹ The SCM Agreement provides Member States with remedies when a subsidy is prohibited under the SCM Agreement and actionable (injuring or causing serious prejudice to the domestic market of a trading partner, or nullifying or impairing benefits under the GATT accruing to a trading partner).⁵²

⁴⁸ Goods are considered dumped and, therefore, subject to an antidumping duty when "the export price of the product exported from one country to another is less than the comparable price, in the ordinary course of trade, for the like product when destined for consumption in the exporting country." Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994 art. 2.1, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1868 U.N.T.S. 201 [hereinafter Antidumping Agreement]. Brazil argues that antidumping duties are inappropriate because they are exporter-specific, and because exchange rates apply across an entire country. Brazil Note, *supra* note 4, at 7–8. While this is a valid concern regarding the efficacy of addressing currency misalignment through antidumping duties, a more fundamental difficulty exists. Namely, currency misalignment is unlikely to be reflected in the dumping margin as misalignment. If Company A sells a product in its home country, Country A, for two Country A Dollars and sells that product to importers in Country B for 1 Country B Dollar, then it is, by definition, dumping if the exchange rate is 1:1. However, if the exchange rate is 1:2, then there is no dumping because the prices are the same once the exchange rate is factored into price, whether the currencies are misaligned or not. See Antidumping Agreement, *supra*, art. 2.4.1.

A safeguard may be imposed when a country experiences such increased imports of a given product that domestic industry is seriously injured or threatened with serious injury. Agreement on Safeguards art. 2.1, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1869 U.N.T.S. 154 [hereinafter Safeguards Agreement]. As Brazil notes, a safeguard must be implemented on a product, not a specific country; therefore, application of safeguards would fail to address bilateral currency misalignment as all countries exporting a good subject to a safeguard measure would be affected by the measure. *Id.* art. 2.2; Brazil Note, *supra* note 4, at 8.

⁴⁹ See Elizabeth Pettis, *Is China's Manipulation of Its Currency an Actionable Violation of the IMF and/or the WTO Agreements?*, 10 J. INT'L BUS. & L. 281 (2011); Mercurio & Leung, *supra* note 31. *But see* Caryl, *supra* note 34; Alusio de Lima-Campos & Juan Antonio Gaviria Gil, *A Case for Misaligned Currencies as Countervailable Subsidies*, 46 J. WORLD TRADE 1017 (2012).

⁵⁰ Simon Lester, *The Problem of Subsidies as a Means of Protectionism: Lessons from the WTO EC—Aircrafts Case*, 12 MELB. J. INT'L L. 345, 369–70 (2011).

⁵¹ Agreement on Subsidies and Countervailing Measures art. 1, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1869 U.N.T.S. 14 [hereinafter SCM Agreement].

⁵² *Id.* art. 4.

In order to prove the existence of an actionable subsidy, a government must provide a financial contribution that confers a benefit to a specific industry.⁵³ Although currency manipulation may distort the competitive playing field, such manipulation may not meet the specificity requirement of the SCM Agreement. This is because, generally, all companies located in a country that undervalues its currency benefit from the Government's currency manipulation because lower currency values allow exporters to undersell foreign competitors.⁵⁴ If all exporters benefit, it is difficult to identify any specific recipient of the benefit.

Furthermore, the expansive notion of currency manipulation introduced by Brazil also raises questions about how currency manipulation is defined. Brazil addresses not only direct manipulation by countries that actively control the value of their currency—what China is often accused of—but also other state interventions that impact exchange rates, such as the U.S. Federal Reserve Bank's policy of quantitative easing.⁵⁵ Brazil's approach seems to be premised on the notion that government interventions that affect currency value confer an unfair competitive advantage. If currency manipulation is defined as state interventions that limit the exchange rate movement of a country's currency, then the possibilities for new types of countervailable subsidies expand dramatically.

III. BRAZIL'S PROPOSAL

To remedy what it perceives as a harmful regulatory vacuum that leads to currency misalignments with adverse impacts on trade, Brazil has called on the international community to address this concern. Specifically, Brazil has raised the issue in the context of the WTO and suggested that filling the exchange rate regulatory gap may require trade remedies.

Brazil argues that the interaction of exchange rates and trade affects every country, and, if not addressed by the international community, countries will begin to craft their own responses to exchange rate distortions, which may lead to tariff wars and increased protectionism.⁵⁶ Furthermore, Brazil, as one of the

⁵³ *Id.* arts. 1, 2.

⁵⁴ Pettis, *supra* note 49, at 294–95 (noting the problem of showing specificity for currency manipulation but arguing that a case could be made against China).

⁵⁵ Rathbone & Wheatley, *supra* note 36.

⁵⁶ See Brazil Note, *supra* note 4, at 6; see also Josué Gomes da Silva, Chief Exec. Officer, Coteminas, Brazil, Presentation at WTO Seminar on Exchange Rates and Trade (Mar. 27, 2012) (presentation slides available at http://www.wto.org/english/news_e/news12_e/news12_e/devel_27mar12_e.htm) (click on the link titled

most prominent voices in the developing world, is not only warning against the downside risk of failing to address the relationship of exchange rates and trade. Brazil is also urging the international community to provide an appropriate institutional framework to promote what it sees as development-oriented trade and finance. As Pakistan points out in a submission in support of Brazil's proposal, "[t]he current thinking presumes that liberalization of trade and market oriented finance policies provide development by themselves."⁵⁷ However, Pakistan goes on to argue that such an approach is insufficient because the harms of unregulated fiscal and monetary policy counterbalance the benefits of access to markets for the developing world.⁵⁸ This sentiment, that liberalization alone is insufficient, captures the Brazilian concern that liberalized financial policies, including exchange rate policies, have negative impacts on trade, particularly in developing countries.

Brazil argues that lower trade barriers, which increase trade opportunities for the developing world, are offset by the rising value of developing world currencies that result from fiscal policies that devalue currencies in the developed world. In its proposal to the WGTDF, Brazil described its concern this way:

Responses to the financial and economic crisis of 2008/09 have included the adoption, by a vast number of countries, of largely similar fiscal expansionist measures coupled with the lowering of interest rates. Yet, differently calibrated mixes of monetary and fiscal policy instruments have caused relative exchange rates among major trading partners to fluctuate frequently, with potentially different long-term impacts on their respective trade balances.⁵⁹

As an example, Brazil has expressed pointed criticism of the U.S. Federal Reserve Bank's practice of placing more U.S. dollars into circulation by purchasing government debt, a practice known as quantitative easing,⁶⁰ and the

"presentation," under Josué Gomes da Silva's name); see also Len Bracken, *Evenett Notes Rise in Protectionism by G-20, Highlights Change in Forms*, 29 Int'l Trade Rep. (BNA) 908, 909 (2012) ("Developing countries have . . . caught up and show no signs of slowing down [in resorting to protectionism].").

⁵⁷ General Council, Preparations for the Fourth Session on the Ministerial Conference, *Proposal of the Establishment of a Working Group for the Study of the Inter-Relationship between Trade and Finance*, paras. 1-3, WT/GC/W/444 (Sept. 18, 2001) (proposal submitted to the WTO).

⁵⁸ *Id.*

⁵⁹ Brazil Proposal, *supra* note 1, at 1.

⁶⁰ For a more thorough description of the Federal Reserve's policy of quantitative easing, see Ben Bernanke, Chairman, Bd. of Governors of Fed. Reserve System, *The Crisis and the Policy Response*, Stamp

effect this practice has had on Brazilian firms' ability to export goods.⁶¹ Brazil argues that the United States' policy of quantitative easing depreciates the value of the U.S. dollar, causing the value of Brazilian currency to rise, and, thereby, impairs growth in Brazil's export market.⁶² Importantly, Brazil's concern over exchange rate fluctuation and currency manipulation is not limited to the recent target of such accusations, China,⁶³ rather, as the foregoing example suggests, it encompasses a broader spectrum of countries and practices.

With these concerns in mind, in April 2011, Brazil proposed that the WGTDF include in its program of activities "the relationship between exchange rates and international trade."⁶⁴ The proposed program has two Pillars. The first Pillar focuses on understanding the nexus between exchange rates and trade.⁶⁵ The second Pillar has an institutional focus and seeks to analyze the application of the Coherence Mandate⁶⁶ and the availability of redress in the multilateral trading system for Member States for distortions caused by exchange-rate misalignment.⁶⁷ The goal of the proposed program is to better understand the impact of exchange rates on trade and their implications for Member States.

On May 10, 2011, WTO members reached a consensus on proceeding with Brazil's proposed first Pillar, including a review of the empirical research and literature on the relationship of exchange rates and trade.⁶⁸ On September 27, 2011, the WTO Secretariat completed this review, which found some evidence pointing to a strong connection between exchange rates and trade, and other evidence showing no connection.⁶⁹ In response to the WTO's survey, the

Memorial Lecture at London School of Economics (Jan. 13, 2009) (transcript available at <http://www.federalreserve.gov/newsevents/speech/bernanke20090113a.htm>).

⁶¹ Tom Miles, *INTERVIEW—Brazil Breaks Currency Taboo at the WTO*, REUTERS, Mar. 26, 2012, available at <http://in.reuters.com/article/2012/03/26/wto-currencies-idINL6E8EN8F120120326>.

⁶² Rathbone & Wheatley, *supra* note 36. Brazil has also criticized quantitative easing programs in other countries such as Japan. *Id.*

⁶³ Brazil has also been highly critical of what it sees as distortive and unfair currency practices by China. *The Controversy over Currency Manipulation*, WASH. TRADE REP., Apr. 2, 2012, at 1, 3.

⁶⁴ Brazil Proposal, *supra* note 1, at 1–2.

⁶⁵ *Id.* at 2.

⁶⁶ For more information on the Coherence Mandate, see *infra* Part IV.B.

⁶⁷ Brazil Proposal, *supra* note 1, at 2–3.

⁶⁸ Working Group on Trade, Debt and Finance, Note by the Secretariat, *The Relationship Between Exchange Rates and International Trade: A Review of Economic Literature*, para. 1, WT/WGTDF/W/57 (Sept. 27, 2011) [hereinafter *Literature Review*] (note submitted to the WTO).

⁶⁹ *Id.* paras. 75–76 (finding that "[o]n the question of the effects of exchange rate volatility on trade, the considerable array of theoretical and empirical literature remains somewhat ambiguous" and that "[o]n the

WGTDF held a seminar in Geneva in March 2012 to discuss the relationship between exchange rates and trade in light of the Secretariat's note.⁷⁰ The seminar featured presentations by representatives of the private sector, public sector, international organizations, and academia.⁷¹

The March seminar proclaimed a general agreement on the existence of a relationship between exchange rates and trade flows.⁷² Specifically, the discussion during the seminar focused on the relationship between trade flows and the misalignment of exchange rates, rather than on exchange rate fluctuation.⁷³ Representatives at the meeting also made clear that it would be difficult to establish measures and assess exchange rates in different countries.⁷⁴ This point confirmed the position of many Member States who believe that the WTO should not get involved in the management of exchange rates.⁷⁵ The discussions during the March seminar did not expressly state what the role of the WTO should be, but the discussions did make clear that there is agreement that the WTO's role is not to manage exchange rates.⁷⁶

While there continues to be significant skepticism about the WTO taking any action on exchange rates and trade, Brazil is pressing forward with its work agenda. On November 5, 2012, Brazil made a follow-up submission to the WGTDF, in which it continued to press for the WTO to address the trade impact of currency misalignment.⁷⁷ As part of this follow-up submission, Brazil put forward a new set of inquiries that would need to be investigated for the WTO to address currency misalignment and suggested that the best course

issue of the level of exchange rates (misalignments), theoretical and empirical studies over the years show that the relationship between the level of a currency and trade is so multi-faceted and complex that it is hard to take a firm line in any particular direction").

⁷⁰ WTO Seminar on Exchange Rates and Trade, WORLD TRADE ORG. (Mar. 27–28, 2012), http://www.wto.org/english/news_e/news12_e/devel_27mar12_e.htm [hereinafter Seminar Program].

⁷¹ For a full schedule of seminar presentations, see *id.*

⁷² Brazil Note, *supra* note 4, at 1; see also Lamy, *supra* note 27; Vera Thorstensen, Lucas Ferraz & Emerson Marçal, *Effects of Exchange-Rate Misalignments on Tariffs*, VOX (Dec. 4, 2011), <http://www.voxeu.org/article/why-wto-should-care-about-exchange-rates>. The parties to the March meeting insisted that the meetings be conducted behind closed doors. Daniel Pruzin, *U.S., Others to Keep WTO Currency Talks Behind Closed Doors*, 29 Int'l Trade Rep. (BNA) 438 (2012). Therefore, much of what we know about the meeting comes from Brazil's most recent submission to the WGTDF. See Brazil Note, *supra* note 4.

⁷³ Brazil Note, *supra* note 4, at 1.

⁷⁴ *Id.* at 1–2.

⁷⁵ See, e.g., *China Objects as Brazil Seeks Discussion on Currency Trade Remedies*, INSIDE U.S. TRADE (Nov. 29, 2012), <http://insidetrade.com/Inside-Trade-General/Public-Content-World-Trade-Online/china-objects-as-brazil-seeks-discussion-on-currency-trade-remedies/menu-id-896.html>.

⁷⁶ Brazil Note, *supra* note 4, at 2.

⁷⁷ See *id.*

would be to create a trade remedy that member states could use to offset the negative impact of currency misalignment.⁷⁸ As of the writing of this Recent Development, there has been no agreement to proceed with Brazil's proposed second Pillar, and some countries have come out against Brazil's recent suggestion for analytical work on a trade remedy.⁷⁹ Nonetheless, Brazil has opened the discussion on exchange rates in the context of the WTO and is committed to pursuing that discussion. In this context it is worthwhile to consider the implications of what Brazil is proposing.

IV. ISSUES AND IMPLICATIONS

While the WTO has not reached an agreement on proceeding to the second Pillar of Brazil's proposal, the proposal itself has introduced a contentious and important debate with potentially widespread implications. The issues identified in the second Pillar—investigating the possibility of redress in the context of the multilateral trading system and resolving issues of coherence with other international institutions—are essential to any movement in addressing exchange rates and trade. Thus, it is important to examine the potential for regulating exchange rates within the current international legal framework and the implication of Brazil's proposal on coherence between the WTO and the IMF.

A. *Defining an Unfair Trade Practice*

Any suggestion that a country should be able to correct for an exchange rate imbalance must address whether exchange rates, like for example labor rates, constitute a factor of trade that should accrue to the benefit of a country. This is especially true when considering the often-made argument that currency devaluation accompanies economic decline and is one mechanism by which a country can halt or reverse its economic fortunes by using the lower prices for its goods to spur exports.⁸⁰ Assuming that such devaluation is not the result of manipulation, on what grounds would the WTO be justified to permit any sort of remedy for such devaluation under its current structure? In other words, how is devalued currency an unfair trade practice?

⁷⁸ *Id.* at 8–9 (“Members may wish, against this background, to consider the need for exchange-rate trade remedies and to start some analytical work to that effect.”).

⁷⁹ *China Objects as Brazil Seeks Discussion on Currency Trade Remedies*, *supra* note 75.

⁸⁰ See, e.g., Paul Krugman, Op-Ed., *Those Revolting Europeans*, N.Y. TIMES, May 7, 2012, at A23; see also R.A., *What Happens After the Fall*, ECONOMIST: FREE EXCHANGE (July 10, 2012), <http://www.economist.com/blogs/freeexchange/2012/07/devaluation>.

Currency manipulation, in contrast, seems to invite a more concrete response in the form of trade remedies. Unlike currency fluctuation, currency manipulation is more easily defined as an unfair trade practice due to the proactive and affirmative rather than reactive and passive involvement by the respective government. Insofar as a state intervenes directly in the value of its currency for the purpose of creating a comparative trade advantage—or, perhaps, even when a state intervenes indirectly with the effect of creating such advantage—this is not an advantage that accrues from its comparative position in the market. However, the latter is not nearly as clear cut a case as the former. An important and difficult question raised by Brazil's proposal is how to determine when an exchange rate imbalance is a legitimate expression of a state's economic reality and when it is an illegitimate intervention by the state. Brazil's notion of currency misalignment does not clearly fall on one side or the other of this conceptual divide. Currency misalignment may capture the seemingly illegitimate notion of currency manipulation, but it also captures fiscal activity that indirectly affects exchange rates. The question of how to determine what types of exchange rate imbalances should be considered unfair trade practices has not been answered.

It may be that the exchange rate imbalance need not be an unfair trade practice to be remedied. Rather, such a remedy could be conceived of in the vein of a safeguard, which is less concerned with the unfair actions of a foreign country than an unexpected negative impact on domestic industry.⁸¹ Safeguards—which are targeted at products not exporters or countries—are distinguished from unfair trade practices because they focus on the effect on a specific industry, regardless of the origin of the effect, rather than the actions of a specific actor.⁸² By contrast, imposition of an antidumping duty or countervailing duty requires a finding that either the exporter or the exporting country has engaged in an unfair trade practice, namely dumping or provision of an illegitimate subsidy.⁸³ Exchange rate imbalances, however, are not like safeguards because an exchange rate imbalance always occurs between two countries and affects all goods from a specific country. A remedy to correct for an exchange rate imbalance would be ineffective if applied irrespective of source because such a remedy must be calibrated to account for the amount of the imbalance caused by a particular country. Likewise, such remedial

⁸¹ See Safeguards Agreement, *supra* note 48, art. 2.2 (noting that a safeguard is to be applied to all imports of the designated product irrespective of source).

⁸² *Id.*

⁸³ See Antidumping Agreement, *supra* note 48, art. 2. See generally SCM Agreement, *supra* note 51.

measures would be futile if applied to a limited array of products because the price of all goods from a country is affected by the exchange rate. Thus, a safeguard-style remedy would be both very broad with regards to products and difficult to apply on a most favored nation basis. Making every imbalance remediable certainly runs up against the question of whether a country should be able to benefit from its devalued currency, as discussed above, and, insofar as such a remedy were only applied selectively there must be some basis, such as an unfair trade practice, for such select application.

The answer to the question of what constitutes a remediable trade practice under current international trade law includes unfair trade practices and specific, serious threats to domestic industry, but there is little guidance on how currency misalignment fits into these categories, in part because such a remedy was rejected during the GATT negotiations.⁸⁴ It may be time to reconsider whether certain policies that result in exchange rate imbalances should be considered unfair trade practices given that the exchange rate regime is now largely unregulated. But, to do so requires weighing the importance of remedying adverse effects on trade against a country's ability to promote other economic policies such as stability and growth.⁸⁵ While there may be real and adverse impacts on trade due to currency misalignments, that does not, in turn, provide a solid theoretical ground for remedying misalignments. This does not mean that there is not a solid foundation for making currency misalignments remediable. However, while Brazil presses forward with analytical work on exchange-rate trade remedies, including the logistics of such a remedy, it would be worthwhile for others to consider how and whether such a remedy could or could not coexist with other remedies in the law of international trade. To answer such a question, in turn, raises the question of coherence.

B. Coherence

As L. Alan Winters notes in his article, *Coherence and the WTO*, coherence between the administrator of the GATT (currently the WTO), the IMF, and the World Bank has been a collective goal of these organizations since their origins.⁸⁶ Coherence is seen as a process with the goal of achieving harmony

⁸⁴ See Brazil Note, *supra* note 4, at 2.

⁸⁵ Consider, in this regard, China's justification for its direct intervention in the value of the renminbi, see *Public Announcement*, *supra* note 33, and the United States' justification for quantitative easing, see *Bernanke Defends Fed Policy*, *supra* note 36, at B2.

⁸⁶ L. Alan Winters, *Coherence and the WTO*, 23 OXFORD REV. ECON. POLICY 461, 462–63 (2007).

between trade, finance, development, and macroeconomic policy.⁸⁷ The Coherence Mandate, adopted at Marrakesh in April 1994, during the negotiations that created the WTO, formalized this goal by directing “Ministers [to] confirm their resolution to strive for greater global coherence of policies in the fields of trade, money and finance, including cooperation between the WTO, the IMF and the World Bank for that purpose.”⁸⁸ The WTO recognizes that, pursuant to the Coherence Mandate, “the WTO system is only one part of a much broader set of international rights and obligations that bind WTO members.”⁸⁹ The Articles of Agreement of the IMF were created to compliment the provisions of the GATT through a coherent set of rules with the goal of achieving “the progressive liberalization of trade and payments.”⁹⁰

In a post-Bretton Woods world, exchange rates continue to fall under the auspices of the IMF, but the IMF has little control over actual rates. Rather, the IMF has the limited power to “exercise firm surveillance over the exchange rate policy of all members and adopt specific principles for the guidance of all members with respect to those policies.”⁹¹ Through the adoption of standards, the IMF may influence Member States’ policy; however, the IMF lacks the authority to compel Member States to comply with its rules or alter exchange rate practices.⁹² Arguably, this creates coherence problems where the adverse impacts of exchange rate policy must be addressed—for example, the adverse impacts on trade that Brazil is alleging—because exchange rates are unregulated and the IMF has no tools for direct intervention.⁹³ Yet, the fact that the IMF’s role is now primarily advisory does not abolish the Coherence Mandate.

⁸⁷ Auboin, *supra* note 8, at 1.

⁸⁸ Marrakesh Declaration para. 18 Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization 1867 U.N.T.S. 148 [hereinafter Marrakesh Declaration]. Along with the Marrakesh Declaration, the WTO and the IMF also signed the Agreement Between the International Monetary Fund and the World Trade Organization recognizing the importance of the Coherence Mandate and agreeing, among other things, to: 1) consult each other regarding the discharge of their respective duties and 2) communicate regarding matters of mutual interest. SANFORD, *supra* note 25, at 4 & 4 n.9; *see also* Int’l Monetary Fund, *Agreement Between the International Monetary Fund and the World Trade Organization*, WT/L/195 (Nov. 18, 1996), compiled in 36 SELECTED DECISIONS AND SELECTED DOCUMENTS OF THE INT’L MONETARY FUND 932 (2011).

⁸⁹ *The WTO and Other Organizations*, WORLD TRADE ORG., http://www.wto.org/english/thewto_e/coher_e/coher_e.htm (last visited Feb. 1, 2013).

⁹⁰ Auboin, *supra* note 8, at 5.

⁹¹ INT’L MONETARY FUND, ARTICLES OF AGREEMENT art. IV, § 3 (2011), available at <http://www.imf.org/external/pubs/ft/aa/index.htm>.

⁹² SANFORD, *supra* note 25, at 2.

⁹³ *See* Winters, *supra* note 86, at 463 (noting that the disparate functions of the GATT, IMF, and World Bank have always contributed to a sense of incoherence, but that early in their existence these institutions operated in more clearly discrete arenas towards different ends).

In addition to the legal limitations of their respective agreements, the varied regulatory approach of the two organizations further complicates inter-institutional cooperation on this issue. The WTO possesses a regulatory enforcement mechanism that functions through an adversarial, bottom-up process. Once a rule is set down under one of the international trade laws, it can be enforced through the WTO's dispute settlement process.⁹⁴ The IMF, in contrast, carries special expertise on currency issues and functions through a cooperative top-down approach.⁹⁵ The IMF strives to maintain financial and exchange rate stability through consultation, technical assistance, and lending.⁹⁶

Brazil's suggestion for trade remedies attempts to avoid the coherence issue by not directly regulating exchange rates. Rather, the proposal would allow states to counteract the negative effect of currency misalignment through something akin to a "currency duty."⁹⁷ In this regard, Brazil is proposing that the WTO, through its Member States, adopt a method for counteracting currency misalignment that fits within the WTO's expertise and institutional structure. However, this does not totally dispel coherence concerns. First, such a remedy would be difficult without the involvement of the IMF.⁹⁸ The unregulated nature of exchange rates means that it is a stretch of authority for any entity to conclude that a currency is not correctly valued. That being said, if any institution has such authority, it is the IMF, and not the WTO or the WTO's Member States.⁹⁹ Establishing a mechanism outside of the IMF would create the possibility of the WTO determining a currency is not correctly valued without the agreement of the IMF.¹⁰⁰ This does not seem to comport with the Coherence Mandate. Furthermore, a currency duty would amount to an indirect method to regulate currency values and exchange rates in the same way that a countervailing duty is an indirect way to regulate certain kinds of

⁹⁴ See generally DSU, *supra* note 47.

⁹⁵ See Cho & Kelly, *supra* note 29, at 528.

⁹⁶ *Id.*

⁹⁷ See Brazil Note, *supra* note 4, at 8–9.

⁹⁸ Brazil recognizes this when it suggests that in establishing methodologies for assessing currency misalignments, "[c]ooperation with the IMF could be explored." *Id.* at 8.

⁹⁹ See SANFORD, *supra* note 25, at 5.

¹⁰⁰ Brazil suggests that establishing currency value for trade remedy purposes "would not be to establish optimal or equilibrium exchange rates for particular currencies, but rather to detect significant departures from historical or reasonable levels." Brazil Note, *supra* note 4, at 8. While a determination of misalignment may not be prescriptive regarding the proper value of a currency, it is a determination that the stated value of the currency is not accurate or legitimate, and such a determination could run afoul of determinations made by the IMF.

discouraged subsidies. Thus, even using a methodology solidly within the WTO's wheelhouse, the implementation of such a methodology means the WTO must move into areas traditionally under the auspices of the IMF. At a minimum, concurrent discussions about such a policy should be underway in the IMF.

CONCLUSIONS

The international response to the Brazilian proposal has been tepid at best. Adding currency fluctuation to the WTO's agenda has not been welcomed in the global arena.¹⁰¹ The possibility of increasing the IMF's authority has been met with similar distaste.¹⁰² The international regulation of exchange rates is generally a sensitive issue amongst international trade partners, because exchange rates are generally a matter of sovereign control. There is some irony to the particular resistance to regulation of exchange rates through the existing international regulatory organizations, given the major role exchange rate stability and trade played in laying the foundation of those same organizations. Irony aside, the disagreement over which institution should regulate the impact of exchange rates on international trade coupled with the disagreement over the nature of the relationship between exchange rates and trade should lead one to surmise that the Brazilian proposal has a tough road ahead. Yet, the conversation that Brazil has begun will continue, for now.¹⁰³

Brazil's proposal is an important development in the arena of international economic regulation. Brazil has highlighted ways in which developing economies may not see the full benefits of increased trade opportunities because of economic developments traditionally considered to be outside the purview of the multilateral trading system. The capacity to recognize and the ability to regulate, however, are two very different things. While it is too early to speak to the efficacy of any proposed resolution, and the hurdles to a negotiated solution are high, it is an important conversation for the international community to have.

¹⁰¹ See Lamy, *supra* note 27 ("All these issues require a mix of cooperation in the macro-financial field and proper domestic policies which lie outside the remit of the WTO. In the current volatile environment, we need to make sure that the WTO system does not crumble under the weight of excessive expectations."); see also China Objects as Brazil Seeks Discussion on Currency Trade Remedies, *supra* note 75.

¹⁰² SANFORD, *supra* note 25, at 5 ("[F]ew countries want the IMF to have the kinds of power over their economies that it would need to compel violators comply with its rules.").

¹⁰³ Daniel Pruzin, *WTO Exchange Rate Seminar Ends with Agreement to Continue Discussions*, 29 Int'l Trade Rep. (BNA) 534 (2012) (noting the general need among participants to continue the discussion, but that no date has been fixed for the next round of discussions).