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Perestroika and Market Socialism: The Effects of Communism's Slow Thaw on East-West Economic Relations

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PERSPECTIVES

***Perestroika* and Market Socialism: The Effects of Communism's Slow Thaw on East-West Economic Relations**

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I. THE NEED FOR A CONSTRUCTIVE EAST-WEST ECONOMIC ENGAGEMENT	214
II. THE COLD WAR HERITAGE: UNEVEN AND UNEASY ECONOMIC RELATIONS	220
III. THE DECADE OF DENG XIAOPING: CHINA'S NEW AWAKENING.....	224
IV. THE ECONOMIC REFORMS OF <i>PERESTROIKA</i> : Precursors to Market Socialism?.....	228
A. Reforms in the Soviet Union	228
1. <i>Labor and Employment Policies</i>	230
2. <i>Quality Control</i>	232
3. <i>Domestic Business Practices in a Centrally Planned Economy</i>	232
4. <i>Price Controls</i>	233
5. <i>Agricultural Reform</i>	234
B. Reforms in Other Eastern Bloc Countries	235

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V.	THE INVESTMENT DIMENSION: NEW SOVIET JOINT VENTURE LAW	238
A.	Negotiations and Formation of the Venture.....	240
B.	Emphasis on Export Industries and Repatriation of Profits	240
C.	Quality Control.....	244
D.	Labor and Employment Problems	245
E.	Limits on Foreign Equity and Control	246
F.	The Bureaucratic Maze	247
G.	Other Considerations	248
	1. <i>Operational Flexibility</i>	248
	2. <i>Conditions for Foreign Workers and Staff</i>	248
	3. <i>Industrial Glasnost</i>	249
	4. <i>Dispute Resolution</i>	249
	5. <i>Liquidation or Nationalization</i>	249
H.	Advantages in Investment in the Soviet Union	250
VI.	THE TRADE DIMENSION	251
A.	Protectionism	252
B.	Match of Market and Plan	252
C.	Admission to GATT.....	254
D.	Technology.....	255
E.	Fiscal and Monetary Reforms	256
F.	Increased Economic Relations with Western Europe and Developing Nations.....	257
G.	Soviet Economic Agencies Restructured	258
VII.	THE HUMAN RIGHTS DIMENSION	260
A.	Glasnost and the "Democratization" Movement	260
B.	The Human Rights-Trade Linkage and Economic Sanctions	263
VIII.	LOOKING TO THE FUTURE: HUMAN RIGHTS ADVANCEMENT THROUGH GREATER INTEGRATION INTO THE WORLD ECONOMIC COMMUNITY	269
IX.	THE GEOPOLITICAL DIMENSIONS AND SOME CONCLUSIONS ABOUT THE PROSPECTS FOR A NEW STRATEGIC ECONOMIC POLICY TOWARDS THE EAST	271
I.	THE NEED FOR A CONSTRUCTIVE EAST-WEST ECONOMIC ENGAGEMENT	

The United States post-war foreign policy towards the East has been dominated by a strategic-military orientation. This Perspective will examine East-West relations from a new perspective, one in which an im-

proved climate of economic relations, based upon mutually beneficial trade and investment contacts between the United States and the major communist nations, provides a complement for diplomatic efforts to reduce global military tensions. The threshold analytical premise of this study is that United States foreign policy must be addressed as a comprehensive whole, and that foreign economic, human rights, political and geostrategic policies are not only interdependent, but indivisible. Decisions about United States foreign economic policy therefore must of necessity flow from an initial assessment of the geopolitical milieu in which strategic issues arise. A gradual shift from a strategic-military orientation to a strategic-economic orientation in United States foreign policy may now be possible because of contemporary changes in the Soviet Union and the People's Republic of China (China). These two communist nations will provide the principal case studies for analysis herein of recent reforms in communist countries and their implications for East-West relations.

Any optimism in the United States business community over the prospects for increased economic relations with the East must, however, be tempered by considerable caution, both from a business perspective and a strategic perspective. Any attempts at economic rapprochement with the communist world, particularly the Soviet Union, should be made from a position of strength, with military, economic, foreign relations and moral strength gathered in concert. The pursuit of a meaningful economic relationship with the East should neither connote nor require a weakening of the defenses of the United States.

In spite of detente and other efforts to break from the cold war heritage of East-West estrangement, the chill has lingered to cast a pall over any attempts at improved economic relations between the United States and the communist world, especially the Soviet Union. Russia's record of extraterritorial ambitions and suppression of human rights is not easily forgotten in the United States, where the fundamental rights of the individual are considered paramount. Throughout most of the seventy years since the communist takeover in Russia, the estrangement has been the hub of United States foreign political and economic policy, but in part because United States strategists have been confined by doctrines developed nearly forty years ago.

United States foreign policy towards the Soviet Union has been based upon the strategy of containment, originally developed by George Kennan during the immediate post-World War II period.¹ It is a matter

¹ The seminal policy statement found in the National Security Council document, "NSC 68" (April 14, 1950), was put into effect at the beginning of the Korean War and was grounded on the

of historical record that the despotic utopia promised by communist theory at times has masked the most ruthless kind of suppression of human rights, particularly as implemented by Lenin and Stalin in the Soviet Union, and later by Mao Zedong in China. The world of 1950 called for a drastic response to halt the spread of communism, which was viewed as a menace to world peace. However, the world has changed dramatically since Lenin, Stalin and Mao Zedong, and the economic and strategic powers, goals and perspectives of the United States have changed along with those of the rest of the world. In recent years, many would argue that the most dramatic changes, political as well as economic, have taken place in some of the leading nations of the communist world.

Among the most telling changes are those reforms that have occurred in China during the decade since Deng Xiaoping came to power. No longer fitting the traditional mold of a socialist economy, China now styles its system as "market socialism," a new system with some marked similarities to capitalism, although retaining its distinctive brand of "socialism with Chinese characteristics."²

More recently, Mikhail Gorbachev has promoted the notion of *perestroika* (restructuring) in the Soviet Union, aimed at rehabilitating the faltering Soviet economy, but also suggesting significant domestic political and foreign policy reforms as well. In his speech on the occasion of the 70th anniversary of the Bolshevik Revolution, he stated that the conflict between communism and capitalism should not be regarded as inevitable; rather, there should be room for cautious cooperation in an "interrelated, interdependent world."³ In his recent book entitled *Perestroika: New Thinking for Our Country and the World*, he achieved an unprecedented public relations coup by addressing a world-wide audi-

fear that the Soviet Union was a bellicose power devoted to expanding world communism, and that it would launch a massive non-nuclear attack (most likely in western Europe). This concern was later exacerbated by the Soviet Union's growing arsenal of nuclear weapons that could be unleashed at the United States. The Eisenhower-Dulles "New Look" (1953-1961) relied upon the deterrent of massive retaliatory power within the context of strategic asymmetry. The Kennedy-Johnson administration introduced the notion of "flexible response" which prevailed until the end of Johnson's term in 1969. Detente was the catchword during the Nixon-Kissinger administration, and was perpetuated by Presidents Ford and Carter until the Soviets invaded Afghanistan in late 1979. Throughout the entire post-war period to date, the notion of containment has prevailed, generally in an atmosphere of mutual East-West hostility.

² Although "socialism with Chinese characteristics" does not represent an abandonment of socialist principles in favor of capitalism, it does reflect a significant departure from the Maoist model (which prevailed during the reign of Mao Zedong, 1949-1976) in favor of modernization. See J. TOWNSEND & B. WOMACK, *POLITICS IN CHINA* 394-95 (3rd ed. 1986).

³ Mikhail S. Gorbachev's address in Moscow on November 2, 1987, on the occasion of the 70th anniversary of the Bolshevik Revolution. 66 FOREIGN AFF. 410, 411 (Winter 1987-88).

ence with what has been widely interpreted as unusual candor.⁴

For a very long time, anyone who challenged perceptions of the Soviet Union as embodied in the strategy of containment was apt to be affixed with a far-left label, or worse yet, branded as pro-communist. Proponents of improved United States-Soviet economic relations may risk a similar fate.⁵ Ideological barriers to any proposals for East-West rapprochement and improved economic and business relations continue to exist. Recently, however, thoughtful observers have questioned some of the long-held perceptions and strategies that have been so fundamental to United States foreign policy.

The changes that have occurred over the past few decades justify such a reassessment.⁶ We no longer live in a bipolar world; rather, the world is multipolar, with constantly shifting alliances. Adherence to the original strategy of containment is proving increasingly costly, not only in financial terms, but in the credibility of United States initiatives in developing countries which are most susceptible to the lure of communism's promise of a utopia, albeit a despotic one.

The significant changes that have evolved in the United States during the past forty years, both on the domestic scene and in our foreign relations, have introduced new factors and circumstances that now demand fresh thinking on our foreign policy options, both in the economic and strategic realms.⁷ In 1950, only the United States had significant

⁴ The wave of Gorbaphilia that rippled throughout the free world in late 1987 created enormous public relations advantages for the Soviet Union. By the end of 1987, Gorbachev's book, *PERESTROIKA*, was a bestseller in many countries of the world, including, for example, Brazil, a country that traditionally has been anti-communist. During Gorbachev's visit to the United States for the summit meeting with President Reagan in December, the Soviet leader mingled with crowds on Connecticut Avenue in Washington, D.C., inspiring one bystander to gush, "It's like the coming of the second messiah, or something." *The Other Power in the Kremlin*, Asian Wall St. J., Dec. 18-19, 1987, at 10, col. 3.

⁵ For example, see Safire, *Let's Make Use of the New Soviet Weakness*, St. Petersburg Times, Feb. 27, 1988, at 1A, col. 1, in which he brands those favoring improved United States-Soviet trade relations as "accommodationists" and "detentniks."

⁶ Paul Nitze, President Reagan's arms control adviser and the original draftsman of NSC 68, recently was quoted as saying, "The assumptions of NSC 68 were not wrong for the time. . . . We thought the Soviet Union would change in a generation. It has taken longer." *Uncle Sam in a Grave* *New World*, U.S. NEWS AND WORLD REP., Jan. 25, 1988, at 46.

⁷ A major problem with the U.S. strategic legacy of indiscriminate response to Soviet aggression is that it suggests apocalyptic thinking that borders on the incredible for the Soviet Union, the United States and our allies alike. In the contemporary world of the late twentieth century, it therefore may fail in its primary mission, to persuade. Richard Perle, *Launching the Right Answer at the Right Question*, U.S. NEWS AND WORLD REP., Jan. 25, 1988, at 47. Without discounting the need for continued vigilance against communist expansionism, a reassessment of our basic strategic policies toward the East now seems highly appropriate. In early January 1988, a bipartisan commission headed by under secretary of defense Fred Ikle and strategist Albert Wohlstetter released a study proposing an entirely new strategy based upon "discriminate deterrence." *Id.* at col. 1. Regardless

deliverable nuclear deterrence. The Soviet Union was not yet even a credible strategic nuclear power, although it soon would have a growing nuclear arsenal. Today, not only is the Soviet Union a formidable nuclear power, but the number of other nuclear powers worldwide has proliferated at an alarming rate.

Domestically, it is the general consensus in Congress that the United States no longer can afford to act as the world's policeman.⁸ A major platform in contemporary political rhetoric, including that of 1988 presidential aspirants, is increased burden-sharing by our allies; Western Europe, Japan, and other nations that stand on potential battlegrounds of communism's advance must assume a greater share of responsibility for their own defense.⁹ Although the notion of increased burden-sharing has a special voter appeal at a time when many of our allies are viewed as enjoying unfair advantages in their trade relations with the United States, it does pose some very troublesome questions. How can this goal be accomplished at a time when conventional defenses in Europe need to be built up?¹⁰ How will the United States counteract the resulting decline in prestige and influence? The doctrine of United States strategic influence abroad is already a major concern as the forward-basing system now appears in jeopardy.¹¹

The United States has shifted focus of its attention abroad. As it has become clear that the Pacific is no longer an "American Lake" and that East Asian economic powers are able to sustain frontal challenges to the United States in world markets, a dramatic shift of attention to the Pa-

of whether or not this innovative report offers a viable alternative to traditional United States strategic thinking, its influence likely will be minimized because it was commissioned by two officials who are no longer in positions to champion the proposal: former Defense Secretary Caspar Weinberger and former National Security Adviser John Poindexter.

⁸ HOUSE ARMED SERVICES COMM., 100TH CONG. 2D SESS., REPORT OF THE DEFENSE BURDENSARING PANEL (Comm. Print 1988).

⁹ In 1986, United States military expenditures represented 6.6% of total output of goods and services. The comparable figures for certain key allies were: United Kingdom (5.1%), West Germany (3.1%), Belgium (2.8%), Italy (2.3%), and Japan (1.0%). *U.S. Candidates Call for Burden-Sharing*, Asian Wall St. J., Mar. 3, 1988, at 1, col. 3.

¹⁰ The negotiation of a conventional force reduction agreement with the Soviet Union appears to be favored, thus placing Gorbachev in a particularly advantageous situation.

¹¹ By the early 1980s, the pressures of nationalism and lures of neutralism threatened to unravel the foreign network of key U.S. military installations. At the end of World War II, the United States had 7,000 foreign installations; in the postwar period, the number was reduced to almost 700, including listening posts and communications facilities. Beginning in 1981, some of our allies (e.g., Greece, Portugal, Spain, Turkey, Philippines, South Korea) began either to complain about the United States presence, or to demand that the United States up the financial ante for maintaining its bases. In some cases, the demand has been that the United States military presence be removed entirely. *U.S. Overseas Military Network Unravels*, Asian Wall St. J., Jan. 7, 1988, at 1, col. 3. See also *U.S. Foreign Policy Outlives its Time*, Asian Wall St. J., Feb. 3, 1988, at 8, col. 3.

cific Rim Basin countries has occurred during the past decade. Similarly, Central and Latin America, which traditionally received little attention in United States strategic thinking, now have become new focal points of United States policy. Our allies in Western Europe, the traditional focus of United States strategic interests, have consolidated their collective economic powers through the European Economic Community ("EEC")¹² and now appear increasingly willing to deal economically with the Soviet Union, even if it means a sharp rebuff of United States foreign policies.¹³

In addressing his western neighbors, Gorbachev now refers to Europe as our "common home",¹⁴ emphasizing the "common European history" that binds Western Europe and the Soviet Union.¹⁵ This theme appears to have a special emphasis in Soviet dealings with West Germany (a key player in NATO's defense structure), where the notion of *Ostpolitik*, or West Germany's political opening to the communist East, is again a priority for Bonn's foreign policy makers and the nation's business executives.¹⁶ The notion of economic isolation and containment of the Soviet Union thus has become increasingly more difficult to imple-

¹² Advocates of an even broader-based European federation are increasingly persuasive, although the unification effort appears to be making little progress. For a good background discussion, see L. BARZINI, *THE EUROPEANS* 23 (1983).

¹³ By 1981, a major conflict had arisen between the United States and its West European allies over the Soviet pipeline issue. Over the strenuous objections of President Reagan, Western European nations entered an agreement with the U.S.S.R. whereby it would finance the building of a Soviet pipeline to supply gas to the West European market. By focusing the attention of these traditional allies on the differences in interests between Western Europe and the United States, the Soviet Union was able to provoke a major confrontation between the United States and some of its traditional allies. See Rosenthal, *The Soviet Pipeline and Its Legal Implications for United States Foreign Policies*, 2 FLA. INT'L L.J. 27 (1986); Rachwald, *The Soviet Approach to West Europe*, CURRENT HIST., Oct. 1983, at 390. One observer was prompted to predict that the prospect of Finlandization of our European allies will occur soon. *United States-Western Europe Relations in 1980: Hearings Before the Subcomm. on Europe & the Middle East of the Comm. on Foreign Affairs*, 96th Cong., 2d Sess. 33 (1980)(statement of Simon H. Serfaty).

¹⁴ M. GORBACHEV, *PERESTROIKA: NEW THINKING FOR OUR COUNTRY AND THE WORLD* 194 (1987).

¹⁵ Some of Gorbachev's recent peace initiatives clearly have been aimed at convincing Western Europeans of Soviet sincerity. The Soviets started withdrawing intermediate-range missiles and troops from Eastern Europe in early 1988, even before the INF treaty had been ratified by both governments. *U.S. Won't Follow Soviet's Lead in Missile Withdrawal*, St. Petersburg Times, Feb. 28, 1988, at 27A, col. 1.

¹⁶ Daumer, *Closing the Identity Gap: The Search for German Unity*, 1988 FLETCHER F. 279, 291. See also Soviets, *Germans Make Overtures as Ostpolitik Comes Center Stage*, Asian Wall St. J., Jan. 20, 1988, at 7, col. 5; *Gorbachev Sways German Missile Town*, Asian Wall St. J., Jan. 8-9, 1988, at 4, col. 4. Simultaneously, Gorbachev is attempting to develop a common Arctic policy with the Nordic countries (including NATO members Norway, Denmark, and Iceland). The Nordic area is of great strategic importance to both NATO and the Warsaw pact. The prospects are good that the Nordic countries will be interested in Gorbachev's suggestions of greater economic and scientific cooperation with the Soviet Union, although the security aspects of the discussions will be more difficult. *Gorbachev Steals a March With Nordic Policy*, Asian Wall St. J., Oct. 14, 1987, at 7, col. 3.

ment, and a reassessment of United States economic foreign policy therefore is timely.

The United States already has determined that it is in our best interests to engage the communist world, particularly the Soviet Union, in a more constructive dialogue to diminish the threat of conflict. A strategy that is yet to be fully explored is the development of a constructive East-West economic relationship that will not only complement, but will accelerate the improvement of strategic relationships.¹⁷

The successful negotiation and ratification in 1988 of the historic United States-Soviet arms reduction treaty¹⁸ therefore not only holds great potential for reduction of military tensions, but also provides a propitious occasion for the reassessment of East-West economic relations. Successful economic ties between the United States and leading communist nations can serve to dispel suspicions and establish a greater international community of interests at least as well as the more newsworthy security treaties. What is needed is a new focus in the United States on strategic economic engagement with the communist world. However, as will be shown, such an engagement is fraught with risks and impeded by very serious obstacles. A threshold task will be to overcome the barriers posed by vestiges of the East-West Cold War heritage.

II. THE COLD WAR HERITAGE: UNEVEN AND UNEASY ECONOMIC RELATIONS

The volume of trade between the United States and communist nations has never been a significant factor in determining United States trade or strategic policies. If the United States is to shift to a new foreign policy towards the East emphasizing improved economic relations, there is very little past experience with the Soviet bloc to offer guidance for government and business. However, United States government and business have had over a decade of successful experience in doing business

¹⁷ Tentative steps towards an economic rapprochement have been initiated. Following the Reagan-Gorbachev summit in December 1987, both nations endorsed expansion of trade and economic relations, and called upon the U.S.-U.S.S.R. Joint Commercial Commission to improve bilateral economic relations between the two countries. *Trade Should Be More Prominent in Next Summit, Commerce Secretary Tells Reporters*, 4 Int'l Trade Rep. (BNA) 1553 (Dec. 16, 1987). The Joint Commercial Commission is composed of senior United States government officials in trade related areas and their Soviet counterparts. The Commission scheduled a meeting in early spring 1988 with the U.S.-U.S.S.R. Trade and Economic Council, an organization of United States companies and Soviet organizations interested in trade, to discuss expanded economic dealings. *Meetings of U.S.-Soviet Joint Commercial Commission, Council Rescheduled for April*, 5 Int'l Trade Rep. (BNA) 331 (March 9, 1988).

¹⁸ *Reagan, Gorbachev Sign Missile-Reduction Treaty*, Asian Wall St. J., Dec. 9, 1987, at 2, col. 1.

with China, and much of this experience may be instructive in the developing economic relationships between the United States and the Soviets.

The United States-Soviet trade balance for the two decades beginning in 1965 was decidedly in favor of the United States.¹⁹ The United States obviously has enjoyed a seller's market during most of this period, primarily because of the Soviet need for grain, which constituted a substantial volume of its imports from the United States.²⁰

On balance, however, United States-Soviet trade has remained relatively modest both in terms of total volume and content. Some of the reasons for this limited level of economic exchange include the absence of most-favored-nation treatment, the linkage of economic policies to political aims, and limitations on exchange of technology for security reasons. Similarly, investment in the Soviet Union has not been a viable option for United States entrepreneurs and financiers for a wide variety of related reasons, including the notable absence, until recently, of a foreign investment law in the Soviet Union.

Geopolitical considerations have continued to occupy center stage in the trade policies of both the United States and the Soviet Union. The cases in which the Soviet Union used the weapon of trade termination in geopolitical disputes with other nations have been amply chronicled,²¹

19

	<u>U.S. Exports to USSR</u> (\$millions F.O.B.)	<u>U.S. Imports from USSR</u> (\$millions F.O.B.)
1965	44	34
1970	119	64
1973	1,192	187
1975	1,834	191
1976	2,306	264
1977	1,621	369
1978	2,249	371
1979	3,604	535
1980	1,510	233
1981	2,357	254
1982	2,589	213
1983	2,002	445
1984	3,283	377

Figures for the period 1965-1979 are from U.N. DEPT. INT'L ECON. & SOC. AFF., U.N. STATISTICAL Y.B., at 448-49, U.N. Doc. No. ST/ESA/STAT/SER.S/7, U.N. Sales No. E/F.81.XVII.1 (1979/80) [hereinafter U.N. STATISTICS]. Comparable figures during 1980-1984 are from U.N. DEPT. INT'L ECONOMICS & SOCIAL AFFAIRS, U.N. STATISTICAL Y.B., at 904-05, U.N. Doc. No. ST/ESA/STAT/SER.S/10, U.N. Sales No. E/F.85.XVII.1 (1983/84).

²⁰ Negotiations on a new U.S.-Soviet grain agreement were scheduled during Spring 1988. Administration officials considered the 1975 and 1983 grain agreements successes in stabilizing grain trade between the two countries. The 1983 agreement expired September 30, 1988. *U.S. Soviet Officials to Meet in Vienna March 11 to Start Talks on New Grain Pact*, 5 Int'l Trade Rep. (BNA) 320, 321 (Mar. 9, 1988).

²¹ JOINT ECONOMIC COMM., 97TH CONG., 2D SESS., SOVIET ECONOMY IN THE 1980S: PROBLEMS AND PROSPECTS, part 1 at 119 (Comm. Print, 1982)(statement of Marshall I. Goldman,

and the use of trade as a political weapon against the Soviets similarly has marred United States-Soviet economic relations for years. Although Eastern European countries have been the Soviet Union's most important trading partners during the post-war period, trade with the West generally has been the most dynamic sector of growth in Soviet foreign trade in recent years in spite of those political problems.²²

In the early 1970s, United States-Soviet trade began to flourish in the hopeful era of detente.²³ Storm clouds gathered quickly, however, beginning in 1974. When the Jackson-Vanik amendment to the Trade Reform Act linked the granting of United States most-favored-nation status with Soviet emigration policies, the United States attempted to use the withholding of trade as pressure against the Soviets.²⁴ The last decade of United States-Soviet relations unfolded with increasingly more serious barriers to an economic rapprochement between the two countries. In 1978, export controls were applied to limit United States sales of oil and gas equipment to the Soviet Union. The motivating reasons were Soviet and Cuban intervention in Africa, and domestic human rights abuses in the USSR. The United States next responded to the Soviet invasion of Afghanistan in 1979 by placing embargoes on grain and fertilizer phosphates, and by tightening export controls on high technology. Additional sanctions were imposed in 1981 when martial law was declared in Poland.²⁵ As will be discussed *infra*, this attempt to use trade privileges as a weapon has not been very successful.²⁶

Changes in Chinese policies, which began over a decade ago, have allowed a different kind of relationship with the West to develop. However, an even more fundamental prerequisite for improved Sino-United States economic relations was the earlier confluence of significant changes in the political and strategic doctrines of both China and the United States. Stung by the United States support of Chiang Kai-shek's Nationalists in pre-1949 China and by its continued support of Chiang's Taipei regime, Mao Zedong was particularly vitriolic in his condemnation of the United States, as communist China increasingly sealed its doors more tightly to economic relations with the West. Throughout

Professor of Economics at Wellesley College and Associate Director of the Russian Research Center at Harvard).

²² Soviet exports to industrialized capitalist countries increased by 55% from 1970 to 1980; Soviet imports from those countries increased by 207 percent during the same decade. Patterson, *Foreign Trade*, in *THE SOVIET UNION TODAY* 213 (2nd ed., J. Cracraft, ed., 1988).

²³ See U.N. STATISTICS, *supra* note 19.

²⁴ The Jackson-Vanik Amendment is discussed at notes 211-12, *infra*, and accompanying text.

²⁵ Patterson, *supra* note 22, at 216.

²⁶ See *infra* notes 211-20 and accompanying text.

most of Mao's regime, economic dealings by United States citizens with China were foreclosed by the Export Control Act of 1949,²⁷ and China virtually was cordoned off by the United States embargo. Having severed its ties with the Soviet Union in a bitter political dispute that began in the 1950s, China became increasingly estranged from both the Western capitalist and the Soviet-bloc communist camps.²⁸

Mao clung to power by increasingly more leftist moves, culminating in the disastrous decade of the Cultural Revolution (1966-1976), during which he unleashed the Red Guards in their lawless pursuit of "counter-revolutionaries" throughout China. There can be no doubt that the leftist abuses which preceded the present Chinese government were sufficient to outrage the conscience of any nation. During the "anti-rightist" campaign, for example, it has been estimated that as many as 700,000 Chinese were arrested, imprisoned, or sentenced to hard labor.²⁹ To keep the ideological flames burning bright, the United States and its so-called "running dogs of imperialism" were fancied by Mao as the enemies of China who had to be kept at bay by eternal revolutionary vigilance. Understandably, the Sino-United States antipathy was mutual for decades under these historical circumstances.

In 1972, President Nixon made his historic visit to China, and China's welcome left the doors of both nations, if not yet fully open to mutual economic relations, at least tentatively ajar. By 1979, when the historic Sino-United States Trade Agreement³⁰ was signed by President Carter's negotiator, China's leadership had passed from the Maoists to a new group of rulers led by the pragmatic reformer, Deng Xiaoping.

Thus, while the Cold War lingered on in United States-Soviet relations, there was a decided warming in Sino-United States relations, particularly in the economic arena. That shift of emphasis not only had significant strategic implications, but also called for a new economic policy orientation in Sino-United States relations. Largely as the result of reforms instituted in China during the most recent decade, Sino-United

²⁷ Export Control Act of 1949, 63 Stat. 7, 50 U.S.C. App. § 2033 (1982), 15 C.F.R. § 385.1(a)(1972). China was given the same trading status as the Soviet Union in 1972. 37 Fed. Reg. 5624 (1972).

²⁸ China was not entirely cut off from trade with the West during this period, and in fact did have commercial dealings with some capitalist as well as communist bloc countries. See G. HSIAO, *THE FOREIGN TRADE OF CHINA: POLICY, LAW, AND PRACTICE* 26-40 (1977). However, it was not until the 1970s that trade with the West began to increase significantly.

²⁹ Weisskopf, *Ex-inmate Recalls Life in China's Gulag*, Washington Post, February 12, 1982, at A1, col. 2.

³⁰ Agreement on Trade Relations Between the United States of America and the People's Republic of China, July 7, 1979, 31 U.S.T. 4651, T.I.A.S. No. 9630 [hereinafter Sino-U.S. Trade Agreement].

States trade and investment have blossomed and provide a useful working model for the development of new strategic-economic thinking about the Eastern bloc states.

III. THE DECADE OF DENG XIAOPING: CHINA'S NEW AWAKENING

During the first decade of his modernization program, which began in 1978, Deng succeeded in implementing both political and economic reforms that would have been unthinkable during Mao's reign. In effect, China has transformed itself from a closed, xenophobic and sometimes ruthless dictatorship to a relatively open, progressive, and eager aspirant for Western-style modernization. There have been periods when it appeared that the leftist wing of China's leadership was again in the ascendency, and the traditional resentment against foreigners resurfaced.³¹ In 1983, for example, the "spiritual pollution" campaign launched attacks on Western influence and ideas, citing the "bourgeois" thoughts and related moral corruption as "anti-socialist" influences.³²

At the 13th Party Congress convened in Beijing in October 1987, further significant political changes were made which may prove the Congress to be a watershed event in the direction of Chinese communism.³³ The principle of separation of party and government was formally adopted, and many of the old-line conservatives stepped aside to allow the ascension to power by younger and more moderate supporters of Deng's modernization program.

The new-style Chinese communism, labeled "market socialism" or "socialism with Chinese characteristics," to take into account the free market inclinations of the new regime, is based upon principles of dependence on economic relations with the capitalist West to help drive China's modernization program. All of this clearly has resulted in a dramatic resurgence of trade between the United States and China. Similarly, United States investment in China has soared in relative terms. The United States is the second largest supplier of investment capital in China, surpassed only by Hong Kong,³⁴ which itself has a predominantly

³¹ The fact that China is now so open and willing to receive western investment and influence is particularly significant in light of China's past exploitation by foreigners. See *Reconciling Human Rights and U.S. Security Interests in Asia: Hearings Before the Subcommittees on Asian and Pacific Affairs and on Human Rights and International Organizations of the House Committee on Foreign Affairs*, 97th Cong. 2nd Sess., 339 (Cong. Print 1982)(Statement of Kenneth Lieberthal)[hereinafter *1982 Hearings*].

³² Seymour, *Spiritual Pollution*, in CHINA RIGHTS ANNALS, 137-43 (J. Seymour ed. 1985).

³³ See generally, Weil, *The 13th Party Congress*, 15 CHINA BUS. REV. 34 (Jan./Feb. 1988).

³⁴ THE NAT'L COUNCIL FOR U.S.-CHINA TRADE, U.S. JOINT VENTURES IN CHINA: A PROGRESS REPORT 2 (1987).

Chinese business community and traditionally has served as China's trade and investment conduit to the Western world.

Direct United States investment in China typically takes the form of contractual joint ventures, equity joint ventures, or wholly foreign-owned enterprises. The equity joint venture is, by volume of investment, the most popular, and was specifically authorized by legislation in 1979.³⁵ The wholly foreign-owned enterprise, which received official Chinese legal sanction in 1987,³⁶ is the least significant to date in terms of total volume of investment capital, but is highly significant in that it represents a further erosion of barriers against purely capitalist enterprises in a socialist state. Each form of investment has received specific protections under China's new legal codes.³⁷

None of this would have been possible without the legal infrastructure that has blossomed in China since 1978. In rapid succession, China has adopted a series of codes to regulate criminal laws, foreign investment, taxation, labor-management relations, domestic and foreign contracts, civil procedure, and other areas of concern to prospective traders and investors. Laws governing domestic relationships among the Chinese citizenry, and between citizens and their government, also have been enacted.³⁸

Some of the subjects of this legal reform have been quite remarkable for a socialist nation, such as the bankruptcy law,³⁹ experiments in estab-

³⁵ Law of the People's Republic of China on Chinese Foreign Equity Joint Ventures, adopted at the Second Session of the Fifth National People's Congress on July 1, 1979, promulgated by Order No. 7 of the Chairman of the Standing Committee of the National People's Congress on and effective as of July 8, 1979. The official English translation is reproduced in 1 *LAWS OF THE PEOPLE'S REPUBLIC OF CHINA (1979-1983)* 150 (1987)[hereinafter Joint Venture Law].

³⁶ Law of the People's Republic of China on Foreign Capital Enterprises, adopted at the Fourth Session of the Sixth National People's Congress, promulgated by Order No. 39 of the President of the People's Republic of China and effective as of April 12, 1986. The official English translation is reproduced in 2 *LAWS OF THE PEOPLE'S REPUBLIC OF CHINA (1983-1986)* 254 (1987)[hereinafter Wholly Foreign Owned Enterprise Law].

³⁷ While there is no law specifically devoted to contractual joint ventures, the law of contractual obligations is found in Law of the People's Republic of China on Economic Contracts Involving Foreign Interests, adopted at the Tenth Session of the Standing Committee of the Sixth National People's Congress, promulgated by Order No. 22 of the President of the People's Republic of China on March 21, 1985, and effective as of July 1, 1985. The official English translation is reproduced in *id.* at 162.

³⁸ For a complete official compilation of Chinese laws passed during the period 1979-1986, see Vols. 1-2 *LAWS OF THE PEOPLE'S REPUBLIC OF CHINA* (1987).

³⁹ Law of the People's Republic of China on Enterprise Bankruptcy (for Trial Implementation), adopted at the 18th meeting of the Standing Committee of the Sixth National People's Congress and promulgated by Order No. 45 of the President of the People's Republic of China on December 2, 1986, for trial implementation three full months after the Law on Industrial Enterprises with Ownership by the Whole People comes into effect. The official English translation is reproduced in 2 *LAWS OF THE PEOPLE'S REPUBLIC OF CHINA (1983-1986)* 289 (1987). The Shenyang Explosion Proof

lishing stock markets,⁴⁰ and agrarian land reform measures which have moved towards the establishment of private property rights.⁴¹ The result has been an emphasis on the rule of law that, at least on its surface, appears more Western than Eastern.

United States businesses have become increasingly more confident about the stability of Beijing's new regime. Although there have been some aberrations which caused potential investors to hesitate, such as Beijing's response to the student demonstrations in early 1987, each passing year has brought new reforms which indicate a consistent course of progress under China's new "market socialism." The 13th Party Congress reaffirmed in October 1987 its commitment to more trade and investment relations with the West,⁴² and other objective indicators suggest it will be a continuing commitment.⁴³

Chinese economic successes during the last decade⁴⁴ generally can be attributed to the coupling of increased decentralization of control with the release of individual initiative through material incentives and freer

Apparatus Factory was the first Chinese enterprise to go bankrupt. Its bankruptcy was recognized under the Trial Bankruptcy Law enacted by Shenyang City, one of three such trial city laws enacted in 1985. *Chief of Bankrupt China Plant Punished*, Asian Wall St. J., Feb. 2, 1988, at 3, col. 4.

⁴⁰ By early 1988, China had set up securities markets in at least six cities. *China to Continue Issuing More Stocks*, Asian Wall St. J., Jan. 13, 1988, at 11, col. 4. However, the "stocks" being sold in China now generally are more in the nature of interest-bearing bonds. In August 1987, Hiway Electrical Co., a small computer systems firm, became the first privately owned company in Beijing to sell shares to the public. *Chinese Shareholders Receive Surprises and a Scolding*, Asian Wall St. J., Feb. 15, 1988, at 1, col. 3. To date, Chinese investors appear to understand little about how true stock investment systems work, and the Chinese system remains small and experimental.

⁴¹ See S. CHEUNG, *WILL CHINA GO 'CAPITALIST'?* 66 (2nd. ed., 1986). In early 1988, experimental regulations were adopted in a number of municipalities which permitted the sale or the transfer of the right to use land. This innovative change, the first time in the history of communist China that the right to use land has been formally recognized as a commodity for sale and purchase, was brought on as a result of foreign investment and other major economic changes during the past decade. *China Lands in the 20th Century*, Asian Wall St. J., Feb. 12-13, 1988, at 6, col. 3.

⁴² Zhao Ziyang, *Advance Along the Road of Socialism With Chinese Characteristics*, Report Delivered at the 13th National Congress of the Communist Party of China on October 25, 1987, 30 BEIJING REV. 23, 32, (Nov. 9-15, 1987).

⁴³ For example, in spite of Party Chairman Hu Yaobang's dismissal in the wake of the 1987 student demonstrations, and the harsh rebuke of the students involved, Beijing continued to issue regulations designed to encourage foreign investment in China. This was particularly significant in view of the fact that Beijing officially placed blame for the demonstrations on "bourgeois liberalism" and the "corruptive" influences of the capitalist West. In Mid-August 1988, China's party leaders and the State Council announced an ambitious five-year plan to further advance economic and political reforms. *Zhao Wins Backing for Reform Strategy*, Asian Wall St. J., Aug. 19-20, 1988, at 1, col. 1.

⁴⁴ The Chinese growth rate of real total product of society rose from 4.6% in 1981 to 13% in 1984. "Total Product of Society" is roughly equivalent to Gross National Product. U.N. ECONOMIC AND SOCIAL COMMISSION OF ASIA AND THE PACIFIC, U.N. ECONOMIC & SOCIAL SURVEY OF ASIA AND THE PACIFIC, at 47, U.N. Doc. ST/ESCAP/405, U.N. Sales No. E. 86.II.F.1 (1985). See also *infra* text accompanying note 66.

market mechanisms. These distinctly capitalist concepts are complemented by greater freedom of choice in economic relations (e.g., in contract relationships⁴⁵ and employment relationships⁴⁶), and by trends which even suggest a movement favoring private ownership of property.⁴⁷ Some observers have concluded that China is moving ineluctably towards capitalism.⁴⁸

Such conclusions may be based more upon wishful thinking than upon realistic assessment of the continuing vitality of socialism in China. In spite of their pro-modernization stance, Deng Xiaoping, Party Chairman Zhao Ziyang, Premier Li Peng and their adherents clearly are ardent socialists in spite of their pragmatism. Moreover, the above reform indicators, although highly significant, are applicable to only a part of China's economic infrastructure. Market socialism in China remains a far cry from capitalism, but it does represent a significant and encouraging departure from the traditional Stalinist-style central planning that continues to impede progress in the Soviet Union.

The message borne on Beijing's example has not been lost on the communist world. Even Vietnam, one of the final holdouts of extreme leftist radicalism, recently passed its own joint venture law and has begun to make overtures to western investors.⁴⁹ While Soviet leaders may not admit that China, their former protege, now is a model for other developing socialist nations, the Soviet Union's own interest in restructuring no doubt has been encouraged by China's successes. Soviet considerations

⁴⁵ Economic Contract Law of the People's Republic of China, adopted at the Fifth National People's Congress, promulgated by Order No. 12 of the Chairman of the Standing Committee of the National People's Congress on Dec. 13, 1981, effective July 1, 1982. *English translation in 1 LAWS OF THE PEOPLE'S REPUBLIC OF CHINA (1979-1982)* 219 (1987).

⁴⁶ See, e.g., *New Labour Market a Success*, China Daily, Aug. 24, 1987, at 3. *Job Interviews Held at Top Polytechnic*, China Daily, July 7, 1987, at 1.

⁴⁷ S. CHEUNG, *supra* note 41, at 67.

⁴⁸ *Id.* at 68.

⁴⁹ Law on Foreign Investment in Vietnam, promulgated by the Council of State of the Republic of Vietnam on Jan. 1, 1988, adopted by the National Assembly of the State of the Republic of Vietnam on Dec. 29, 1987. *English translation reprinted in FOREIGN BROADCAST INFORMATION SERVICE, VNA CARRIES NEW FOREIGN INVESTMENT LAW (East Asia, FBIS-EAS-88-007)* Jan. 12, 1988, at 47. The new law, which reportedly is one of the more liberal foreign investment laws in the communist world, guarantees full repatriation of profits and non-nationalization of investment; sets no limits on the amount of equity held by the foreign partner; guarantees representation of both partners on the management board in proportion to investment; provides for joint appointment of the chairman of the board; and sets the tax rates at 15%-25% of earned profits, with two year tax holidays available. *Vietnamese Promulgate Reforms To Increase Western Investment*, Asian Wall St. J., Jan. 13, 1988, at 3, col. 1. See also *Perestroika, doi moi, Shall We Call The Whole Thing Off*, THE ECONOMIST, Mar. 11, 1988, at 35. Despite the United States sanctions against Vietnam, and Vietnam's continued aggression in Cambodia, some United States allies already are making overtures to establish an investment beachhead there. See, e.g., *Korean Firms Seek Foothold in Vietnam*, Asian Wall St. J., Feb. 5-6, 1988, at 1, col. 4.

of the Chinese example run the gamut of political, economic, and geo-strategic concerns. Sharing thousands of miles of common border with the Soviet Union, and possessing potentially enormous land forces, a rapidly modernizing China not only can serve as a positive example for the Soviets, but as a source of fear and apprehension as well. The vision of a strong Chinese nation with more than one-quarter of the world's population, growing economically in the footsteps of Japan and the other Pacific Basin success stories, and perhaps even becoming militarily and strategically aligned with the United States in the process, must have given great pause to Soviet strategists.

Will the current reform movement in the Soviet bloc enjoy the same successes as the earlier reforms in China? Will those successes enable the United States to develop a new strategic-economic orientation to the Soviet Union and Eastern bloc countries, as it has with China? These are some of the questions raised by an analysis of the Soviet reforms under *perestroika*.

IV. THE ECONOMIC REFORMS OF *PERESTROIKA*: Precursors to Market Socialism?

A. Reforms in the Soviet Union

While market socialism has been, on balance, a major success story in China, Soviet-style communism has been a failure economically. The Soviet annual economic growth rate declined from 5.0% in the late 1960s to 3.0% in the early 1970s. By the late 1970s, it had further declined to 2.3%.⁵⁰ Therefore, Mikhail Sergeyevich Gorbachev was uniquely positioned to alter his nation's destiny. By the time he capped his rapid ascent to power with his appointment as General Secretary of the Communist Party of the Soviet Union (CPSU) in March 1985,⁵¹ pressure for reform was already building within the Party leadership. At the 27th CPSU Congress held in Moscow from February 25 to March 6, 1986, views began to crystalize and a reform consensus arose from the debate; *perestroika* was underway.⁵² During the past two years, Gorbachev has begun to translate the rhetoric of *perestroika* into concrete actions. From late 1986 through early 1987, the Soviets announced significant policy decisions to legalize private labor,⁵³ authorize the establishment of in-

⁵⁰ CENTRAL INTELLIGENCE AGENCY, HANDBOOK OF ECONOMIC STATISTICS, 1986: A REFERENCE AID 64 (1986).

⁵¹ *The Education of Mikhail Sergeyevich Gorbachev*, TIME, Jan. 4, 1988, at 18.

⁵² See M. GORBACHEV, *supra* note 14, at 60-63.

⁵³ In November 1986, a law was passed to legalize the undertaking of individual labor by housewives, students, and pensioners. Additional laws were passed to authorize larger groups to form

dependent cooperatives,⁵⁴ and authorize foreign investment joint ventures.⁵⁵

Additionally, the movement seeks to implement economic reforms that also may facilitate better United States-Soviet trade and investment exchanges. The leaders of the Soviet Union could no longer disguise their disappointment over domestic economic failures and faltering international influence with their traditional techniques of anti-Western rhetoric. As the economy increasingly became more deeply mired in its own Brezhnevian inertia, the utopian society envisioned by Marx and Lenin seemed ever more distant. But it was Gorbachev who seized the initiative of power and opportunity to articulate what was known already by perceptive leaders of the Soviet State: restructuring of the Soviet Union was essential.

The political reforms now being sought in the Soviet Union under the rubric of *perestroika* can, if successful, provide a climate for improved East-West strategic and economic relations. Gorbachev has revealed that he views foreign policy as a continuation of domestic policy,⁵⁶ and it logically follows that he is taking a more conciliatory step in terms of East-West relations in order to carry out his internal policies of *perestroika*.

Gorbachev has focused on improvement of the nation's economic situation as the immediate priority.⁵⁷ Among the economic changes being undertaken in the current Soviet restructuring process, five principal changes are critical: enterprises are being given more expression, the nature and extent of central planning is being altered, efforts are being made to decontrol prices, credit markets are being created, and competition among enterprises is being encouraged. To only develop the Soviet Union with a "half-loaf" philosophy, however, as has been the case with Yugoslavian economic reforms, likely will create uncontrollable difficulty. Success will depend upon an aggressive pursuit of capitalist-style reforms such as those undertaken in China during the past decade. This may be asking too much for the highly ideological Soviets.

How should all of this affect prospective trade and investment relations with the western world? A realistic assessment of the promises of *perestroika* can be achieved by analyzing its goals within the context of the real obstacles Gorbachev will face both within the existing Soviet

service cooperatives. Further legislation authorized state enterprises to enter into contracts with outside individuals. J. HOUGH, *OPENING UP THE SOVIET ECONOMY* 49-50 (1988).

⁵⁴ *Id.*

⁵⁵ See *infra* note 87 and accompanying text.

⁵⁶ *Special Report: Moscow's Vigorous Leader*, *TIME*, Sept. 9, 1985, at 29.

⁵⁷ M. GORBACHEV, *supra* note 14, at 27.

system and abroad. Comparisons with the Chinese reform experience also will be instructive. Following are analyses of only a sampling of the economic and legal challenges confronting Gorbachev's implementation of *perestroika*.

1. *Labor and Employment Policies*

A principal focus of *perestroika* is the motivation and release of the productive energies of the masses.⁵⁸ In theory, communism is based upon a highly egalitarian society in which the state is the ultimate protector and provider for the strong and weak, able and disabled alike. Taken to its extremes, however, this theory quashes individual initiative because it removes those distinctions, monetary and otherwise, that drive individuals to achievement.

Although this weak link in communist theory has had a debilitating impact on the Soviet system, the paradigm of this weak link in communist theory can be found in Mao Zedong's "iron rice bowl" system in China. Under that system, the state provided equally for hard workers and slackers alike, thus removing material incentives for achievement. Achievers were at various times even branded as "counterrevolutionaries" and punished for their bourgeois ways. Ideological incentives, slogans, exhortations, and constant indoctrination eventually wore thin and productivity fell into a state of long-term stagnation. A similar malaise has seized Soviet society, tightening its grip ever more fiercely with the Russian penchant for drowning trouble and depression in great quantities of vodka.

The Chinese have repudiated Mao's "iron rice bowl" theory, and officially have recognized that such extreme egalitarianism is not in the best interest of the people or state. Material incentives have been introduced in China through various economic reforms. The earliest major reform in Deng's regime was the responsibility system in agriculture,⁵⁹ which encouraged individual gain through the exercise of entrepreneurial

⁵⁸ Gorbachev has observed that:

We have come to the conclusion that unless we activate the human factor, that is, unless we take into consideration the diverse interests of people, work collectives, public bodies, and various social groups, unless we rely upon them, and draw them into active, constructive endeavor, it will be impossible for us to accomplish any of the tasks set, or to change the situation in this country.

Id. at 29. Early reports on the progress of reform indicate that for the first time in years, 1987 increases in production could be attributed to higher labor productivity, rather than growth of the work force. *Many Soviet Firms Posting Losses*, *Asian Wall St. J.*, Jan. 26, 1988, at 4, col. 2.

⁵⁹ Officially sanctioned in 1978, the responsibility system in agriculture quickly caught on because it brought immediate success, sometimes more than doubling or tripling agricultural output in one year. Essentially, it has evolved into a system whereby the state leases land to peasants or households who in turn are free to market their produce after paying dues to the state for land usage.

qualities. The responsibility system has been so phenomenally successful in agriculture that the state is now experimenting with its application to industry.

Another type of responsibility system, designed to motivate lackadaisical workers in the massive state enterprise system, is China's new labor contract system.⁶⁰ Workers are no longer guaranteed lifetime employment by the state; rather, each worker is placed on an individual contract under which he is guaranteed employment only for a certain term of years, subject to both renewal and dismissal for cause. By 1987, China's state enterprises employed approximately 93 million employees, with 80% of them on "permanent" worker status. The new contract worker scheme is being phased in as new workers are hired.⁶¹ In short, China has not entirely solved the problem of worker motivation, but it has made significant progress.⁶²

In the Soviet Union, Gorbachev's reform efforts likewise are aimed at motivating workers (and at eliminating contributing factors of worker lethargy, such as the high level of vodka consumption). However, reform efforts thus far have relied principally upon the traditional communist tools of rhetoric and exhortation. It remains to be seen whether that rhetoric will be translated into tangible actions.

In order to provide a workforce for foreign joint venturers that will meet international standards of quality control and productivity, labor and employment issues of the most sensitive kind must be addressed, even to the extent that the extreme egalitarianism of communist theory is challenged. So long as all workers are treated equally in terms of income, regardless of performance, the economy will never thrive. Material incentives must be introduced on a larger scale, with reduced reliance upon the ideological incentives that have proven so ineffective in the past.

Similarly, the notion that the state provides full employment must be abandoned and the concept of a "labor market" must be introduced.

See generally, A. KHAN & E. LEE, *AGRARIAN POLICIES AND INSTITUTIONS IN CHINA AFTER MAO* (1983).

⁶⁰ Interim Regulations on the Implementation of Labor Contracts in State Owned Enterprises, July 12, 1986, reprinted in *Renmin Ribao (People's Daily)*, Sept. 10, 1986, at 2, col. 1, *English translation reprinted in* FOREIGN BROADCAST INFO. SERVICE (FBIS-CHI-86-186) Sept. 25, 1986, at K1-K7 (hereinafter Labor Contract Regulations). See generally, Lewis and Flesher, *China Charts a New Course for Labor*, EAST ASIAN EXEC. REP., March 1987, at 9; *Peking Issues New Labor Regs*, Asian Wall St. J., Sept. 10, 1986, at 13; *China's Value Theory of Labor*, Asian Wall St. J., Sept. 4, 1986, at 157.

⁶¹ *Contract Workers Play Bigger Role*, China Daily, Oct. 17, 1987, at 4, col. 1.

⁶² For a detailed examination of current labor reform efforts in China, see Vause & Vironis, *China's Labor Reform Challenge: Motivation of the Productive Forces*, 24 STAN. J. INT'L L. 447 (1988).

So long as large numbers of surplus employees are over-assigned to state jobs, wage rates will continue to be low, minimizing monetary incentives. On the other hand, if the worker-to-task ratio becomes smaller as the result of more efficient workers who are motivated by material incentives, the state will face an unemployment problem. Although communist countries traditionally have masked their unemployment problems for ideological reasons, it will be one of the harsh realities the Gorbachev regime must face if it expects true progress in labor reform.⁶³

2. *Quality Control*

Related to the problem of low worker motivation is quality control. The quality of products produced in communist countries generally has been notoriously poor. This is due in part because state producers enjoy monopoly power and are not subjected to domestic competition, but also because they do not participate actively in world markets, and then thereby escape the pressures of world competition as well.

3. *Domestic Business Practices in a Centrally Planned Economy*

Economic reform under *perestroika* contemplates restructuring of the way Soviets do business, both domestically and internationally. As is typical in communist countries, the massive bureaucracy is a major impediment to economic efficiency. The movement of goods, supplies, and raw materials; the allocation and distribution of energy and other resources; access to markets, mobility of labor, adjustment of prices, determination of product lines, and virtually every other decision in the chain of sourcing, production and distribution are encumbered by a distant and impervious bureaucracy.

The perpetuation of central control and all its economic aspects, such as subsidies to industries engaged in export production, preclude the Soviet Union from acceptance into the major free-market organizations of the world, such as the General Agreement on Tariffs and Trade (GATT) and the International Monetary Fund (IMF).

Moreover, the inherent inefficiencies of the Soviet bureaucratic state doom the country to the status of a second- or third-rate world economy. It is a one-dimensional world power, basing its international strength primarily on its military forces. It is already clear that the restructuring

⁶³ China's unemployment problem is exacerbated by its rapidly growing population of 1.2 billion. It has attempted to absorb its growing unemployment by encouraging the growth of private enterprises, including rural non-agricultural enterprises. By the end of 1986, more than 18 million people were engaged in private enterprise. *China's Private Business Becomes "Indispensable"*, China Daily, Apr. 11, 1987, at 1, col. 1.

process will take time to implement. The Soviet State Committee for Statistics has reported that during 1987, more than 13% of the nation's factories and economic enterprises operated at a loss, economic organizations failed to meet quality-improvement goals, and factories have been slow to innovate.⁶⁴ *Perestroika*, or some version of innovative reform yet to be announced, appears to be the only salvation for the Soviet economy.

4. Price Controls

In order to be successful, Gorbachev must institute price reforms which not only challenge orthodox communist thinking, but which risk raising the ire of the general populace as well. This challenge may prove to be one of the weakest links in the chain of reform measures. The irrational Soviet price system, which is a major impediment to progress, did not develop randomly, but rather is the result of deliberate planning. The problem is particularly critical in the politically sensitive area of agricultural products pricing. The urban proletariat which long has been appeased by unrealistically low bread and meat prices will react strongly to any price hikes. And yet, such market-oriented price adjustments appear absolutely essential to true domestic reform.

China at least tentatively has addressed the problem of price reform, but is finding it difficult to implement desired changes.⁶⁵ During 1987, China's gross national product increased 9.4%.⁶⁶ However, Chinese sources reported that the annual inflation rate as measured by retail prices was almost 8% in 1987, and may exceed 10% in 1988.⁶⁷ By early 1988, China's Central Bank announced plans to cut the money supply sharply during 1988 in an effort limit excessive demands that have pushed inflation up during the past year.⁶⁸ The price control/inflation dilemma no doubt will provide ammunition for the extreme conservatives for years to come as they challenge reform efforts in both countries, but mastery of this dilemma remains an essential goal if reform efforts are to be successful.⁶⁹

⁶⁴ *Many Soviet Firms Posting Losses*, Asian Wall St. J., Jan. 26, 1988, at 4, col. 2.

⁶⁵ Pressed by the growing crisis of low grain yields due to continued low prices, Beijing has been forced to consider further reforms in agriculture. Ignatius, *Beijing Weighs Changes in Agriculture*, Asian Wall St. J., Jan. 26, 1988, at 1, col. 4.

⁶⁶ Schiffman, *China's GNP Grows 9.4%, but Inflation Takes Its Toll*, Asian Wall St. J., Feb. 24, 1988, at 3, col. 1.

⁶⁷ *China's Inflation Rises*, Asian Wall St. J., Jan. 29-30, at 19, col. 4.

⁶⁸ *China to Cut Money Supply to Combat Rising Inflation*, Asian Wall St. J., Jan. 14, 1988, at 3, col. 1.

⁶⁹ In mid-August, 1988, the Party announced its "Tentative Plan on the Price and Wage Reforms" for 1989-1993. The price and wage reforms are considered the key to the entire process of

5. *Agricultural Reform*

The challenges of price reform are particularly acute in agriculture. Neither the Soviet Union nor China will achieve needed agricultural sector reforms until agricultural prices are brought into greater alignment with the forces of supply and demand. In contrast to China, where structural reform in agriculture was one of the first agenda items for Deng Xiaoping in 1978, the Soviets have done very little to reform the critical agricultural sector. Gorbachev should understand the need for such reform because he became intimately acquainted with the problems of agriculture while he was Central Committee Secretary for Agriculture under Brezhnev.⁷⁰ Part of the problem is the strong Soviet ideological commitment to collectivization in agriculture.⁷¹ The 1986 reforms that allowed collective farms to sell fruit and vegetables directly to the consumers at higher prices than the state stores was a significant improvement, although not a major structural reform. In contrast, China has not only allowed free agricultural markets to develop, but has abandoned Mao's communal approach to agriculture and encouraged the formation of individual agricultural plots.

In short, the solutions to the economic problems of the major communist countries appear to be capitalistic in nature: (1) introduction of labor incentives coupled with an abandonment of communist-style economic egalitarianism; (2) substantial relaxation or abandonment of rigid central planning; (3) introduction of market mechanisms in pricing, income distribution, material sourcing, and distribution of goods; and (4) active engagement of enterprises in competitive domestic and world markets.

The steps already taken in these directions have not been easy adjustments for China, but while it still has far to go, it has made remarkable progress in a mere decade. For the Soviet Union, the adjustment no

economic restructuring in China, and their success in turn depends upon a further deepening of the overall economic reform effort. *Politburo Accepts 1989-1993 Price Reform Outline*, China Daily, Aug. 19, 1988, at 1, col. 1.

⁷⁰ It should be noted that Gorbachev made no major policy changes in agriculture when he served as head of agriculture under Brezhnev. He did support the expansion of a contract system whereby certain resources were assigned to teams of workers who in turn were compensated based upon their output. However, this system has not been very effective in increasing output or in containing rising costs of production. Johnson, *Agriculture*, in *SOVIET UNION TODAY* 208 (2nd. ed., J. Cracraft ed. 1988).

⁷¹ In contrast, the Chinese have enjoyed a major success in agricultural reform because they have largely displaced the collectivization commitment of Mao Zedong with a "contract responsibility system" which virtually establishes leaseholds from the State to the peasants, whereby the lessees are totally responsible for their own success, and keep all the profits from their production, less a usage fee paid to the State. See Vause & Vironis, *supra* note 62.

doubt will be even more difficult, because it has not shown the ideological flexibility that China has, and Soviet citizens have virtually no experience with capitalist concepts. A major distinguishing factor between the Soviet Union today and China in 1978 is that reform at the grass roots level virtually was waiting to happen in China when Deng Xiaoping began to aggressively pursue his reforms. China already had gone through ten years of trauma during the cultural revolution, which provided a profound historical testament for the ills of extreme leftism. The new leadership only needed to loosen the reigns and set free the market instincts of the Chinese people. The remarkable reforms in Chinese agriculture came from the peasants themselves; the government and party simply allowed it to happen. Soviet citizens have not had an experience comparable to the cultural revolution to propel the people away from leftism. Gorbachev himself has admitted that *perestroika* is an attempt to impose a "revolution from above."⁷² Introduction of market mechanisms will mean that the Soviet consumers will vote with their rubles, and, the complexity of making the transition from the centrally planned, state dominated and controlled economy to this new form of economic democracy will be enormous.

As complex as reform in the Soviet Union may be, reform throughout other sectors of the Eastern bloc is even more variegated and uneven. This intensifies the difficulty facing Gorbachev, for the success of reforms in Eastern Europe will have a significant influence on the tenure of reformist leadership in the USSR.

B. Reforms in Other Eastern Bloc Countries

A significant danger to *perestroika* is that Gorbachev will not be able to move far enough and fast enough to make a lasting difference before the immediate disadvantages of reform (e.g., inflation, price hikes, worker umbrage under increased responsibility and decreased job security) begin to stall the reformists' momentum. An ambivalent position between the traditional centrally planned economy and a market economy will be difficult to sustain, as shown by the example of Yugoslavia.

Yugoslavia has made significant changes, both politically and economically, during the last quarter of a century. Politically, decentralization has been accompanied in Yugoslavia by greater liberalization. It is the only Eastern European country that allows its citizens to emigrate

⁷² What is meant is profound and essentially revolutionary changes implemented on the initiative of the authorities themselves but necessitated by objective changes in the situation and in social moods.

It may seem that our current *perestroika* could be called a "revolution from above."

M. GORBACHEV, *supra* note 14, at 55.

freely, bringing more openness to outside influence than other East European nations under Soviet influence. However, the country does remain firmly Marxist-Leninist, under the control of one party.

In the economic arena, substantial decentralization has occurred and worker participation has been increased. However, because of ambivalence towards the establishment of a true market economy, economic reform has on the whole not been very successful. Although the economy has been changed, the government has held back and stopped short of fundamental reforms, in contrast to the fundamental reforms now being pursued by China.⁷³

Ironically, the greatest promise of reform in the Eastern bloc was ended by the Soviets twenty years ago when Leonid Brezhnev sent tanks and 650,000 Warsaw Pact troops into Czechoslovakia on August 20, 1968 to crush the "Prague Spring" of sweeping reforms that had flowered under Alexander Dubček.⁷⁴ Although the country remains scarred from the Soviet lesson administered two decades ago, it now is instituting both political and economic reforms, with Gorbachev's blessings, under the new leadership of Milos Jakeš.⁷⁵ Jakeš proposes to abandon excessive economic centralization; promote the adoption of advanced technologies; seek greater industrial cooperation and joint ventures with West European countries; expand the rights and responsibilities of state enterprises and make them accountable, self-financing and self-managing; give the workers greater involvement in management selection; and encourage growth in productivity through the use of economic incentives.⁷⁶

While Czechoslovakia is contemplating sweeping reforms, Hungary has already instituted many and is considered the most reformist in the bloc.⁷⁷ Economic reforms include a new tax system, including sales taxes on consumer goods and a progressive income tax with a top rate of 60%. Massive reductions in subsidies to state industries will put thousands out of work, a politically sensitive step that not even Moscow has been willing to take. Political reforms are so far-reaching that the future of the Communist Party is now being debated, with some talk of permitting opposition parties.⁷⁸ Hungary already has a foreign joint venture law, and United States Commerce Department figures show that there are about 150 Hungarian joint ventures with Western firms, ten of which are

⁷³ See *Taking Glasnost Seriously*, Asian Wall St. J., Dec. 9, 1987, at 8, col. 3.

⁷⁴ *Breezes from Moscow*, TIME, Apr. 18, 1988, at 41.

⁷⁵ *Id.* at 42.

⁷⁶ Jakeš: *'We Simply Need Restructuring'*, TIME, Apr. 18, 1988, at 42.

⁷⁷ *Breezes from Moscow*, *supra* note 74, at 42.

⁷⁸ *Id.*

with United States organizations.⁷⁹ The nation's lawmakers also are considering a new "Law on Economic Organizations," which is expected to be passed by the end of 1988, and which would further liberalize opportunities for foreign investors. Hungary reportedly is interested in increasing trade with the United States.⁸⁰

Bulgarian efforts to show Moscow that it too is reforming have been so vigorous that bureaucracies reportedly are confused over national priorities.⁸¹ The actual changes thus far have been relatively modest, such as the allowance of free markets to spring up for vegetable farmers.⁸² In sharp contrast to Bulgaria, Rumania appears resistant to *perestroika* under the rule of Nicolae Ceaușescu, who stubbornly maintains policies that keep Rumania as the bloc's poorest country. With the economy in ruins, the country's greatest hope for reform probably lies in Ceaușescu's successor.⁸³

Poland also faces widespread hardship, but for different reasons. In spite of a series of economic reforms that have been instituted since 1983, real income and standard of living remain about the same as 1975 levels. Poland suffers from sporadic electrical blackouts, has the largest external debt in the Eastern bloc, has an inflation rate of 35%, and is experiencing a "brain drain" as hordes of university graduates leave the country. Party leader Wojciech Jaruzelski, who reportedly is the leading liberalizer and close ideological ally to Gorbachev,⁸⁴ will enjoy success in his economic reform efforts only when political reforms are effected as well.

East Germany has shown considerable resistance to Gorbachev's political ideas, principally because it already has enjoyed a significant record of economic success through central planning.⁸⁵

The challenge of developing a United States response to the recent reform efforts in the Soviet Union and other Eastern bloc communist countries must of necessity be addressed in a multi-dimensional context. Some of the geostrategic dimensions of that challenge were discussed in Part I above. Additional dimensions that lie more in the economic realm include those involving foreign investment and trade. The recent reversal of the Soviet attitude respecting foreign investment on Soviet soil poses an immediate opportunity for a United States response. That re-

⁷⁹ *Proposed Hungarian Economic Reform Law Likely to be Discussed During Grosz Visit*, 5 Int'l Trade Rep. 1013 (July 13, 1988).

⁸⁰ *Id.*

⁸¹ *Breezes from Moscow*, *supra* note 74, at 42.

⁸² *Id.*

⁸³ *Id.*

⁸⁴ *Id.*

⁸⁵ *Id.*

ponse will be made largely by United States businesses, based upon the attractiveness of the Soviet investment environment.

V. THE INVESTMENT DIMENSION: A NEW SOVIET JOINT VENTURE LAW

Investment in the Soviet Union may not be viewed as an attractive alternative for many western businessmen because of the anti-Western Soviet government attitude of the past and the lack of appropriate guarantees and protections provided by the Soviet government today. Although there is nothing to suggest that *perestroika* heralds a movement to market socialism, however, it at least has opened the possibility of significant movement away from the rigid, centrally controlled, and anti-western business environment of the past.

On January 13, 1987, the Council of Ministers⁸⁶ of the USSR passed a decree establishing a foreign joint venture law which represents a significant departure from the traditional hostility towards foreign capitalists operating on Soviet soil.⁸⁷ On the same date, the Presidium of the USSR Supreme Soviet⁸⁸ passed an implementing edict.⁸⁹ These actions represent the first time since 1930, when the Soviets canceled all foreign joint ventures, that foreigners have been permitted to engage in joint ven-

⁸⁶ Under the Soviet constitution, the Council of Ministers is "the highest executive and administrative body" of the Soviet State. Konst. SSSR art. 128, (*reprinted in* J. HAZARD, CONSTITUTIONS OF THE COUNTRIES OF THE WORLD 40 (1978); A. UNGER, CONSTITUTIONAL DEVELOPMENT IN THE USSR 258 (1982).

⁸⁷ The January 13, 1987 Council of Ministers decree "On Procedures for the Creation and Operation in the USSR of Joint Enterprises in which Soviet Organizations and Firms from Capitalist and Developing Countries are Partners" was first published in Pravda. *In the USSR Council of Ministers*, Pravda, Jan. 27, 1987 at 2, col. 1 (Eng. ed., Associated Publishers, Inc.). In the United States, the Bureau of National Affairs (BNA) published an English translation of the Council's decree. *Soviet Council of Ministers Decision on Joint Ventures with Western Firms*, 4 Int'l Trade Rep. (BNA) 358-61 (Mar. 11, 1987). An English translation of the Council's decree also was published by the American Society of International Law. *Union of Soviet Socialist Republics: Decree on Joint Enterprises with Western and Developing Countries*, 26 I.L.M. 749 (1987)[hereinafter Soviet Joint Venture Law]. See generally, Carpenter and Smith, *U.S. Soviet Joint Ventures: A New Opening in the East*, BUS. LAWYER 79 (1987); Comment, *Foreign Investment: New Soviet Joint Venture Law*, 28 HARV. INT'L L.J. 473 (1987).

⁸⁸ The Russian Constitution defines the Supreme Soviet as "the highest body of state authority." Konst. SSSR art. 108, *reprinted in* J. HAZARD, *supra* note 86, at 37; A. UNGER, *supra* note 86, at 258.

⁸⁹ The English translation of the January 13, 1987 Supreme Soviet Edict "On Questions Connected with the Creation on the Territory of the USSR and the Activity of Joint Enterprises, International Associations, and Organizations with the Participation of Soviet and Foreign Organizations, Firms, and Agencies of Administration" is published by the American Society of International Law. *Union of Soviet Socialist Republics: Edict Concerning Taxation of Joint Enterprises in the Soviet Union and Dispute Settlement*, 26 I.L.M. 759 (1987)[hereinafter Soviet Joint Venture Law].

tures in the USSR.⁹⁰ The stated objectives of the new law are to satisfy more fully the country's need in certain kinds of industrial products, raw materials and foodstuffs; to attract to the USSR advanced foreign technology and know-how, managerial expertise and additional material and financial resources; to expand export potentialities and reduce dispensable imports. In summary, the Soviets seek to satisfy many of the same developmental needs as those addressed in 1979 by the Chinese joint venture law.

By the summer of 1987, over 100 western firms had their joint venture proposals under discussion with the Soviets, with letters of intent signed by 70 companies, including 10 United States firms.⁹¹ Reportedly, the Soviets already had signed agreements with five companies from Finland, West Germany, and Japan.⁹²

However, the rush of prospective United States investors to China likely will not be duplicated in the Soviet Union, in spite of its recent efforts to lure western capital. For one thing, the Soviets offer no promise of the warm reception held out by the Chinese, which suggests that they have not yet awakened to the fact that they are suitors who need the investment more than investors need another site.⁹³ Secondly, the disappointments of many who accepted the Chinese invitation likely will have a dampening effect on enthusiasm for investing in yet another socialist economy.⁹⁴ The following analysis summarizes some of the problems and opportunities for prospective investors under the new Soviet joint venture law.

⁹⁰ For a general discussion of earlier Soviet experiences with joint ventures, see Berman, *Joint Ventures Between United States Firms and Soviet Economic Organizations*, 1 INT'L TRADE L.J. 139 (1975-76); Pederson, *Joint Ventures in the Soviet Union: A Legal and Economic Perspective*, 16 HARV. INT'L L.J. 390 (1975).

⁹¹ Testimony of Dep. Asst. Secretary of Commerce for Europe, Franklin J. Vargo, before the International Economic Policy and Trade Subcommittee of the House Foreign Affairs Committee, July 14, 1987. "Jackson-Vanik Resolution on MFN Benefits Not Likely to be Relaxed, Administration Says," 4 Int'l Trade Rep. (BNA) 903, 904 (July 15, 1987). Combustion Engineering Company of the United States already has entered into a joint venture arrangement with the Soviets. *Joint Venture for Instrumentation, Controls, Software Set up by U.S. Firm, Soviet Ministry*, 4 Int'l Trade Rep. (BNA) 1425 (Nov. 18, 1987).

⁹² *Id.*

⁹³ The continued refusal by the United States to grant most favored nation treatment to the Soviet Union may be a factor affecting Soviet hospitality. Yuri Scherbina, President and Chairman of the Board of Amtorg Trading Corp., hinted on January 21, 1987 that Soviet most favored nation status would be a condition of preferences extended to prospective joint venturers. *Soviet Union: Moscow's Joint Venture Law to be Published Shortly, Amtorg President Says*, 4 Int'l Trade Rep. (BNA) 98 (Jan. 28, 1987).

⁹⁴ *China's Economic Reforms Don't Impress Foreigners*, Asian Wall St. J., July 27, 1987, at 3, col. 1. *But cf.*, *China Market Still Attracting U.S. Firms*, Asian Wall St. J., Feb. 12-13, 1988, at 8, col. 1.

A. Negotiations and Formation of the Venture

Seasoned investors in China can attest to the frustrations of negotiating a new investment agreement in a communist country that has little experience with western investment. Westerners should be prepared for the frustrations of lengthy negotiations which likely will be the prerequisite for consummation of any significant deals.⁹⁵ Without a successful past history of dealings, upon which mutual trust can be founded, each party likely will approach the other with considerable caution. Moreover, the legal infrastructure for foreign investment is only sketchy at best. The myriad of commercial and legal details that are taken for granted as resolved by laws in Western countries will be up for negotiation between the parties. Implementation of foreign joint ventures will be an exercise in faith and creativity, if prior domestic reforms in the Soviet Union are any guideline.

Even the easiest of the reforms - privatization of a substantial part of the services sector - required an almost unimaginable array of decisions about business licenses, the setting up of optimal tax rates, rules of business operations, definitions of business expenses for taxation purposes, safety standards and non discrimination rules, consumer protection measures, the establishment of reliable supply system, etc.⁹⁶

The assimilation of foreign investment enterprises into the Soviet system will raise a much larger array of extremely complex questions before a smooth accommodation can be realized.

The nonconvertibility of the ruble will raise many difficult questions when the financial aspects of the investment are negotiated. For example, how will the relative contribution levels of foreign and Soviet equity contributions be valued? The same kinds of problems will arise at the point of liquidation, and will be exacerbated by the fact that the Soviets do not yet recognize the "capitalist" concept of capital gains.⁹⁷

B. Emphasis on Export Industries and Repatriation of Profits

A major motivation behind the new Soviet joint venture law is their shortage of hard currency.⁹⁸ Because the ruble is not convertible on international markets, the Soviets find it necessary to export to acquire

⁹⁵ On May 2, 1988, McDonald's Restaurants of Canada Ltd. announced that a new joint venture agreement had been concluded with the Food Service Administration of the Moscow City Council after 12 years of negotiations. *McDonald's Hamburgers Coming to Soviets Under Agreement with Moscow City Council*, 5 Int'l Trade Rep. (BNA) 672 (May 4, 1988).

⁹⁶ J. HOUGH, *supra* note 53, at 46.

⁹⁷ See *id.* at 84.

⁹⁸ *Soviet Trade: The Bear Facts*, THE ECONOMIST, Feb. 14, 1987, at 57; Ross, *Foreign Investment: New Soviet Joint Venture Law*, 28 HARV. INT'L L.J. 473, 479 (1987).

hard currency necessary to buy needed imports. They earn between 60% and 80% of their hard currency from energy exports, with the figure closer to 80% in recent years.⁹⁹ A hard currency crunch followed the 1986 plunge in the international prices of oil and natural gas, and hard currency exports fell from about \$32 billion in 1984 to about \$25 billion in 1986.¹⁰⁰ The resulting cutback in imports requiring hard currency adversely affected industrial projects already in progress.¹⁰¹

Thus, the Soviet goal of export expansion, while it is a major reason behind the new law, inherently poses barriers to the prospective foreign investment partner gaining access to the huge untapped Soviet market.¹⁰² Although the Soviet market does not have the same aura of romance that the Chinese market had, it can be more desirable in some respects because a large industrial infrastructure already exists in the Soviet Union.¹⁰³ The Soviet export expansion goal is articulated as an export requirement in the new joint venture law. Joint ventures are required to export their products to earn the hard currency needed to pay foreign suppliers and profits to foreign partners.¹⁰⁴ A United States company therefore may not gain much access to the Soviet market if required to export in order to realize a profit.

The new Soviet joint venture law exempts the enterprise from the national economic plan.¹⁰⁵ The joint venture will not be subject to state production plans, but neither will it have any guarantee for product sales.¹⁰⁶ However, its suppliers and purchasers will be operating under Gosplan¹⁰⁷ production and sales plans.¹⁰⁸ Purchases and sales by the joint venture on the Soviet market are to take place through Soviet for-

⁹⁹ Zabijaka, *Soviet Foreign Trade Reforms Offer New Challenges for U.S. Business*, BUS. AM., Aug. 17, 1987, at 6; *Joint Ventures in Russia: Comrades in Profit?*, THE ECONOMIST, Dec. 20, 1986, at 91; *Soviet Trade: The Bear Facts*, THE ECONOMIST, Feb. 14, 1987, at 56.

¹⁰⁰ Zabijaka, *supra* note 99, at 6.

¹⁰¹ *Id.*

¹⁰² Carpenter & Smith, *U.S. Soviet Joint Ventures: A New Opening in the East*, 43 BUS. LAW. 79, 80 (1987).

¹⁰³ Brady, Galuszka, Javetski & Pearson, *Reforming the Soviet Economy: After the Summit, Gorbachev's "Restructuring" Will Face a Stern Test*, BUS. WK. Dec. 7, 1987, at 84 [hereinafter Brady, Galuszka].

¹⁰⁴ Soviet Joint Venture Law, art. 27, *supra* note 89, 26 I.L.M. at 754.

¹⁰⁵ Soviet Joint Venture Law, art. 23, *supra* note 89, 26 I.L.M. at 754. See also Dun, *The New Soviet Joint Venture Regulations*, 12 N.C.J. INT'L L. & COM. REG. 171, 174 (1987).

¹⁰⁶ Soviet Joint Venture Law, art. 23, *supra* note 89, 26 I.L.M. at 754.

¹⁰⁷ Gosplan is the state planning agency responsible for production plans. See Dore, *Plan and Contract in the Domestic and Foreign Trade of the U.S.S.R.*, 8 SYR. J. INT'L L. & COM. 29, 32 (1980).

¹⁰⁸ Ross, *Foreign Investment: New Soviet Joint Venture Law*, 28 HARV. INT'L L.J. 473, 477 (1987).

eign trade organizations.¹⁰⁹ Therefore, the Soviet foreign trade organizations will have control over the joint venture's ability to purchase necessary supplies and to sell its products in the Soviet market.

Again, the joint venture will find that success is dependent on producing a product necessary for economic recovery. If the joint venture product fits a category targeted for cooperation, the venture's ability to buy and sell in the Soviet market will be enhanced. The foreign trade organizations will become assets in predicting Soviet demand for the product and in marketing it. But if the product is not one targeted for economic recovery, then the foreign trade organizations may favor exports over domestic sales and protect Soviet industries competing with joint ventures. They also may contend that the venture's proposed purchases and sales do not mesh with the state production and sales plans for Soviet suppliers and purchasers.

One of the major problems that surfaced early in the Chinese foreign joint venture enterprises was Chinese insistence on manufacture of products for export only, coupled with tight restrictions on repatriation of capital. It was not until one of the largest early investors, American Motors Corporation, threatened to withdraw from its investment in China's Beijing Jeep Ltd., that concessions on currency exchange and repatriation of capital were ordered by China's top leadership.¹¹⁰ The Soviet joint venture law clearly encourages export industries, and will offer little opportunity for access to the Soviet domestic market.¹¹¹

One proposed solution for the repatriation of profits issue is for the Soviets to allow those joint venture enterprises producing "import substitution" products for domestic consumption to convert their rubles income into international currency for repatriation purposes. Problems will exist, of course, in defining what products are actually designed for "import substitution."¹¹²

Some Western companies have already designed creative solutions to these marketing goal conflicts between Soviets and Westerners. As of November 1987, eleven joint venture agreements had been signed with

¹⁰⁹ Soviet Joint Venture Law, art. 24, *supra* note 89, 26 I.L.M. at 754.

¹¹⁰ See Vause, *China's Developing Auto Industry: An Opportunity for American Investors—and Challenge for China's New Legal System*, 10 PENN. J. INT'L BUS. L. — (1988), for a review of the difficulties faced by American Motors Corporation, and opportunities that have since developed in the Chinese auto industry. The Soviets recently initiated preliminary talks with Ford Motor Co. regarding several Soviet proposals on joint venture arrangements. *Preliminary Ford Motor Co.-Soviet Talks Could Lead to Possible New Joint Venture*, 4 Int'l Trade Rep. (BNA) 1585 (Dec. 23, 1987).

¹¹¹ One noteworthy exception likely will be in the area of services, such as hotels and other businesses that cater to western tourists and businessmen, because the income predominately will be in convertible foreign exchange.

¹¹² See J. HOUGH, *supra* note 53 at 69.

the Soviets, and one half of those were with West German companies.¹¹³ Some of the West German companies based the anticipated success of their projects on creative marketing and capital investment techniques. West Germany's Heinemann machine tool factory agreed to train fifty Soviet technicians for one year, who then will return to Moscow to use their experience at a second plant there.¹¹⁴ By setting up two plants, Heinemann expects to be able to get its profits out of Moscow. According to plans, the products of these plants will find markets both in the Soviet Union and in the West.¹¹⁵ A West German magazine publisher, Verlag Aenne Burda, plans to obtain circulation rights for its dressmaking magazine in the Soviet Union in exchange for building a printing press for use by both the magazine and Soviet enterprises.¹¹⁶ The German company will use its ruble profits to buy Soviet lumber, which will be sold to Western paper producers. A West German petrochemicals producer and a Soviet petrochemicals maker have been negotiating the construction of a plant in the Soviet Union, to be financed by a German bank loan.¹¹⁷ The two firms, Mineralol Rohstoff Handell and Nizhnekansk, will produce ethylene glycol and ethylene oxide and will export half of the output.¹¹⁸

A United States corporation, Monsanto, is negotiating with the Soviets for the output of a chemical herbicide plant to be sold only in the Soviet Union.¹¹⁹ The hard currency requirement will be met by purchasing more of their raw materials from the Soviet Union or by exporting intermediate products from the Soviet plant.¹²⁰ Therefore, Monsanto should be able to gain access to the Soviet market and earn hard currency by exporting.

Another United States company, Cumbustion Engineering Inc., finalized a United States-Soviet joint venture in November 1987, with the Soviet Ministry of Oil Refining and Petrochemical Industry.¹²¹ The company has already dealt with the Soviets for ten years and was the first

¹¹³ Brady, Galuszka & Lewald, *Ivan Starts Learning the Capitalist Ropes: Western Partnerships Are Teaching Soviet Managers the Rules*, BUS. WK., Nov. 2, 1987, at 154.

¹¹⁴ *Id.*

¹¹⁵ *Id.*

¹¹⁶ *Id.*

¹¹⁷ *Id.*

¹¹⁸ *Id.*

¹¹⁹ Brady, Comes & Galuszka, *Soviet Union: Letting Western Business In*, BUS. WK., Apr. 20, 1987, at 40.

¹²⁰ *Id.*

¹²¹ Galuszka & King, *The Twain Are Meeting and Cutting Deals*, BUS. WK., Dec. 7, 1987, at 88; Barlas, *Soviets Court Joint Ventures*, BUS. MARKETING., May 1987, at 38.

United States company to finalize a joint venture with them.¹²² Applied Engineered Systems, the new venture, will manufacture oil and petrochemical process controls for Soviet refineries and assist in modernizing management of plants and refineries.¹²³ The company will take its profits mostly in gasoline and diesel fuel, which will be supplied by the increased yield of modernized refineries.¹²⁴

A United States foreign investor thus may resolve the Soviet-Western firm marketing goals conflict issue by, for example, (1) producing a product with a market both in the Soviet Union and the West so it can take profits in the joint venture product; (2) using ruble profits to purchase Soviet raw materials either for the company's own use or for resale in the West; or (3) exporting intermediate products of production. Successful western joint venture proposals suggest a greater Soviet flexibility concerning the hard currency requirement when the product involved is one they consider necessary for economic recovery. Such products specifically include, "chemicals, such as pesticides, dyeing agents, fibers, various types of machinery, and machinery for pulp and paper, consumer and food industries."¹²⁵ No joint ventures in mining will be authorized.¹²⁶ Therefore, a prospective investor initially should determine whether its joint venture product fits one of these categories. If not, the company probably will not be able to gain immediate access to the potentially huge Soviet market.

C. Quality Control

The low quality of workmanship and poor worker performance that Gorbachev is battling on the domestic front will also handicap joint ventures in their efforts to market quality products for competitive international markets. Foreign joint ventures in China have in many cases been successful in introducing quality control techniques, and similar successes should be realized with Soviet workers. Because the Soviets are newcomers to joint venture arrangements with Westerners, and will need time to adapt and modify Western management techniques and technology to their own local conditions, a lag time of many years may be needed for the Soviets to catch up on the learning curve.

¹²² Galuszka & King, *supra* note 121, at 88.

¹²³ *Id.*

¹²⁴ *Id.*

¹²⁵ Zabijaka, *supra* note 99, at 8.

¹²⁶ *Id.*

D. Labor and Employment Issues

The new Soviet joint venture law states that labor matters will be controlled by Soviet legislation.¹²⁷ The venture must negotiate a contract with the trade union organization, with the contents to be determined by Soviet law.¹²⁸ The wages, hours, vacations, social security and insurance for Soviet employees also are to be "regulated by Soviet law."¹²⁹ Of course, Soviet law should apply to these issues, but these requirements are problematical because Soviet law does not address these issues in the detail needed by prospective investors.¹³⁰

In order to maintain efficiency in production, a certain degree of selectivity in hiring, training, and retention necessarily will be applied by joint venture enterprises. Disciplinary rules and procedures must be established. Western companies may find that Soviet workers do not adapt readily in a profit oriented enterprise, and disputes over discipline are bound to surface. Soviet workers take job security for granted, leading some commentators to observe that communism in the Soviet Union has created the "iron borscht bowl of guaranteed employment and all its attendant disincentives for productivity."¹³¹ This Soviet expectation of continued employment, regardless of performance, may be as difficult to break as the "iron rice bowl" has been in China.¹³²

In contrast, one of the stimuli for increased foreign interest in Chinese joint venture opportunities was the promulgation of regulations and procedures on labor and employment.¹³³ In the absence of such guidelines, investors in the USSR will be well advised to negotiate detailed agreements on labor regulation. A host of unanswered questions are raised by the Soviet joint venture law, such as the freedom to select, hire, train, transfer, assign, discipline, and discharge employees; the responsibility for unemployment and workers' compensation obligations; the role

¹²⁷ Soviet Joint Venture Law, art. 20, *supra* note 89, 26 I.L.M. at 757.

¹²⁸ *Id.*

¹²⁹ *Id.*

¹³⁰ *Cf. infra* notes 133, 134 (more detailed provisions in Chinese laws and regulations on the subject of labor management relations).

¹³¹ Klingenberg and Pattison, *Soviet Announcement Should Stir Interest of U.S. Corporations*, *Legal Times*, Mar. 2, 1987, at 13, col. 1. The Soviet Joint Venture Law does not stipulate the employer's right to hire, layoff, discipline or discharge for reasons of efficiency or productivity.

¹³² *See supra* notes 57-63, and accompanying text.

¹³³ Provisions of the People's Republic of China on Labour Management in Joint Ventures Using Chinese and Foreign Investment, July 26, 1980, *English translation reprinted in CHINA INT'L ECONOMIC CONSULTANTS, INC. CHINA INVESTMENT GUIDE 1986* at 470 (1985)[hereinafter JV Labor Regulations]; Procedures for the Implementation of the Provisions for Labour Management in Joint Ventures Using Chinese and Foreign Investment, Dec. 24, 1983, *English translation reprinted in CHINA INT'L ECONOMIC CONSULTANTS, INC. CHINA INVESTMENT GUIDE 1986* at 471 (1985)[hereinafter JV Labor Procedures].

of unions in the enterprise; the level of benefits required by law; the application of minimum and maximum wage requirements imposed by the State; the role of financial incentives; and the ability of foreign enterprises to attract skilled workers and technicians away from State enterprises. Although some of these questions were answered by laws and regulations in China,¹³⁴ many were worked out in practice, and still other questions remain unresolved.

E. Limits on Foreign Equity and Control

The Soviet law poses other limitations which are designed to limit foreign control. For example, it limits the foreign investor's interest to no more than 49%, and requires that the chairman of the board and general director of the enterprise be Soviet citizens.¹³⁵ Yugoslavia was the first country in Eastern Europe to authorize foreign joint ventures in 1967.¹³⁶ Yugoslavia soon learned, however, that a restrictive cap on equity ownership limits the interest of prospective investors, and the Yugoslavian joint venture law was changed to allow western equity interests to go as high as 70%.¹³⁷ The Chinese joint venture law, passed in 1979, only requires that the foreign joint venturer's equity investment "shall be, in general, not less than 25%" of the venture's total registered capital.¹³⁸

More recently, China promulgated the Wholly Foreign Owned Enterprise Law, authorizing foreign firms to establish enterprises exclusively with foreign investment capital.¹³⁹ Although it is not likely that the Soviets will liberalize their investment policies as quickly as the Chinese have, changes in the Soviet law will be needed to increase the attractiveness of Soviet joint venture investment for large western firms.¹⁴⁰

¹³⁴ See, e.g., Provisions of the State Council of the People's Republic of China for the Encouragement of Foreign Investment, Oct. 12, 1986, art. 15, *English translation reprinted in* FOREIGN BROADCAST INFO. SERVICE, CHINA REPORT, Oct. 15, 1986, at K2; Regulations Governing Employment Autonomy, Workers' Wages and Insurance and Welfare Fees in Foreign Investment Enterprises, Nov. 1986, *English translation reprinted in* FOREIGN BROADCAST INFORMATION SERVICE, Dec. 3, 1986, at K5.

¹³⁵ *Soviet Council of Ministers Decision on Joint Venture with Western Firms*, 4 Int'l Trade Rep. (BNA) 358, at 359 (Mar. 11, 1987).

¹³⁶ Buzescu, *Joint Ventures in Eastern Europe*, 32 AM. J. COMP. L. 407, 408 (1984); See also Scriven, *Joint Venture Legislation in Eastern Europe: A Practical Guide*, 21 HARV. INT'L L.J. 633 (1980).

¹³⁷ *Joint Venture Proposal Needs Improvement, 'Full of Loopholes,' Armco Executive Says*, 4 Int'l Trade Rep. (BNA) 130 (Feb. 4, 1987).

¹³⁸ Chinese Joint Venture Law, *supra* note 35, art. 4.

¹³⁹ Chinese Wholly Foreign Owned Enterprise Law, *supra* note 36, art. 4.

¹⁴⁰ The supposed advantages to the Soviets in domination of joint venture management are questionable: "There is little evidence to support the hypothesis that the benefits of foreign investments, such as the transfer of technology, are achieved better when domestic investors are in the majority." Statement of William Ryrie, Executive Vice President of the International Finance Corp., an arm of

Western investors will be particularly reluctant to enter joint ventures under such foreign equity ownership limitations where the venture calls for transfer by the western firm of substantial advanced technology or know how. The importance of controlling ownership also is underscored by the requirements of the Overseas Private Investment Corp. (OPIC) that the United States partner own at least 50% of foreign joint venture investments.¹⁴¹

F. The Bureaucratic Maze

The problems of dealing with the Stalinist style Soviet bureaucracy will be a much more formidable task than most western businessmen will be able to tolerate. Domestically, the entrenched bureaucracy is one of the most formidable challenges Gorbachev now faces.

The China experience is instructive. In 1980, Deng Xiaoping identified the bureaucracy as "a major and widespread problem in the political life of our Party and state."¹⁴² In spite of Beijing's increased efforts to minimize the adverse impact of bureaucracy on foreign investment enterprises, the Deputy Director of the Foreign Investment Bureau at the Chinese Ministry of Foreign Economic Relations and Trade has admitted that the worst problem is interference in day to day joint venture operations by China's legions of bureaucrats. For example, officials often will remove Chinese managers without giving notice or explanation to the foreign partner. As decentralization has progressed in China, local cadres have become even more independent in taking such arbitrary action.¹⁴³

For those with little or no experience with communist bureaucracies, the notorious discrepancy between paper promises of the central government and bureaucratic realities at the local level can pose a trap for the unwary that likely will not be discovered until after the investment has been made. Gorbachev no doubt recognizes this, for he has already identified the bloated and inefficient bureaucracy as a major target of reform.¹⁴⁴ After ten years of reform effort in addressing the same

the World Bank, quoted in *Developing Nations Urged to Ease Investment Rules*, Asian Wall St. J., Jan. 26, 1988, at 17, col. 1.

¹⁴¹ OPIC insurance automatically ends when U.S. ownership of foreign investment enterprises falls below 50%. Under the Reagan administration's proposals, the limit would be lowered to 45%. *House Panel Okays OPIC Reauthorization Bill Similar to Reagan Administration's Proposal*, 5 Int'l Trade Rep. (BNA) 573, 574 (Apr. 20, 1988).

¹⁴² *Reform of System of Party, State Leadership*, China Daily, July 1, 1987, at 4, col. 1 [hereinafter *Reform of System*].

¹⁴³ "Many cadres still hold 'leftist' ideas and see investors as predators." *Japanese Increase Investments in China*, Asian Wall St. J., Feb. 12-13, 1988, at 1, col. 3.

¹⁴⁴ M. Gorbachev, *supra* note 14, at 89-92.

problem, China is yet to resolve the dilemma.

Because the state must be directly involved in each transaction, a threshold problem will be simply identifying all of the national, provincial and municipal agencies involved in licensing and approval processes. An important first step was taken recently when the national Soviet Ministry of Foreign Trade, Committee on Foreign Economic Ties, was delegated increased authority; it apparently will serve as the general contractor for foreign construction inside the Soviet Union.¹⁴⁵ If the Chinese experience provides any lessons in foreign investment management, however, a great deal more needs to be done in streamlining and defining the foreign investment bureaucracy, including greater decentralization of control.

G. Other Considerations

1. *Operational Flexibility*

Related to the problems posed by the omnipresent Soviet bureaucracy will be a host of operational issues. Will the venture have access to raw materials and supplies at reasonable prices?¹⁴⁶ Will delivery schedules be reliable? To what extent will the enterprise have the flexibility to contract with other firms? Will it have discretion in its choice of suppliers? To what extent can the enterprise insist on higher quality supplies and raw materials? Will the enterprise be independent in its decision to terminate, modify, or introduce new product lines? Will the enterprise have independence in modifying annual production plans? To what extent will the enterprise indirectly be locked into the central State plan because of planning limitations on suppliers and purchasers? The myriad of questions relating to labor and employment issues, discussed above, also must be addressed in the context of operational needs. These questions are illustrative only, but they do suggest the wide range of issues that must be addressed by pioneering investors in the USSR.

2. *Conditions for Foreign Workers and Staff*

One of the most frequently voiced complaints from western businessmen living in China, particularly during the early years of joint ven-

¹⁴⁵ J. HOUGH, *supra* note 53, at 63.

¹⁴⁶ Unsatisfactory results in the sourcing of supplies is only one example of an obstacle that, standing alone, could make a foreign investment unprofitable. In view of the difficulties already faced by domestic concerns in the implementation of the new Soviet reforms in this regard, positive assurances should be obtained in advance on supply and material sourcing issues. See *Economist Urges U.S. Firms to be Cautious When Approaching Joint Venture Possibilities*, 5 Int'l Trade Rep. (BNA) 119 (Jan. 27, 1988).

ture investments there, is the inconvenience and inordinately high price of accommodations. China has made great progress in this regard during the past decade, although hotel accommodations for westerners continue to be among the highest priced in the East. Because the Soviet Union has a more highly developed infrastructure, it should be able to avoid many of the problems of housing. Related questions will be the extent to which westerners can staff joint venture enterprises with their own western employees, pay them western level salaries, and obtain entrance visas with ease.

3. *Industrial Glasnost*

Both in the initial negotiations and start up phase, as well as the operational phase, foreign partners will need to obtain access to industrial and market information in the Soviet Union. The extent to which such information is made available to foreign businessmen in this traditionally closed society will be a major factor in assessing the desirability of doing business in the USSR. For foreign joint venturers, this kind of "industrial *glasnost*" can have a significant impact on encouraging western investment.¹⁴⁷

4. *Dispute Resolution*

The Soviet Joint Venture Law provides that dispute resolution be conducted in Soviet law courts or, upon agreement between the two sides, by an arbitration tribunal.¹⁴⁸ It is presumed that the arbitration tribunal will be the Soviet Arbitrazh, which likely would be unacceptable to a United States company due to its orientation toward the state and the state plan.¹⁴⁹

5. *Liquidation or Nationalization*

The Soviet Joint Venture Law gives the USSR Council of Ministers the authority to liquidate the joint venture if its activities do not conform to its original objectives.¹⁵⁰ The risk of liquidation may be heightened by

¹⁴⁷ Another problem for foreign investors, even if a higher degree of industrial *glasnost* is realized, is that Soviet data is not always reliable. It recently was alleged that the use of fraudulent statistics actually has accelerated during Gorbachev's reign. *Soviets Pad Economy With Fiddled Data*, Asian Wall St. J., Feb. 5-6, 1988, at 4, col. 4. This should not be attributed to Gorbachev, but rather to the long tradition of manipulating data in communist states to meet centrally mandated goals.

¹⁴⁸ Soviet Joint Venture Law, art. 20, *supra* note 89, 26 I.L.M. at 753.

¹⁴⁹ Dunn, *The New Soviet Joint Venture Regulations*, 12 N.C.J. INT'L L. & COM. REG. 171, 177 (1987).

¹⁵⁰ Soviet Joint Venture Law, art. 51, *supra* note 89, 26 I.L.M. at 758.

political risks having nothing to do with the venture's own successes or failures. Joint ventures may become less attractive, and therefore more vulnerable, if Gorbachev's economic reform initiatives are unsuccessful and hard line conservatives reassert control. Similar results could follow if United States-Soviet peace initiatives suffer major setbacks. However, either scenario assumes major reversals in United States-Soviet relations, and bad faith in Soviet interpretation of the liquidation clause. Such negativism generally is not fruitful, particularly as it now would be based upon unfounded assumptions.

Barring some major international or domestic upheaval, it also seems highly unlikely that nationalization of foreign investment enterprises in the Soviet Union will be a significant risk. Stability and respect in the international community apparently is very high in the present hierarchy of Soviet values, particularly as it seeks membership in GATT and other international economic organizations. As greater stability is achieved in the overall United States-Soviet relationship, especially through increased economic dealings, this risk should be further minimized.

H. Advantages in Investment in the Soviet Union

Although the challenges facing prospective western investors will be many, the anticipated rewards nevertheless may attract firms that will see opportunities under the new Soviet joint venture law. Some will wish to establish a beachhead in the Soviet Union based on the theory that those who enter the market early and become "old friends" of the Soviet business and government communities will reap long term benefits. Those firms that are taking a long term view of their relationship with the Soviet Union will want to get in early to build up experience in dealing within the Soviet system.

Some firms will see the opportunity to gain a foothold in the potentially enormous Soviet domestic market. The domestic market, however, appears not to be an opportunity in the immediate future for very many firms, because the Soviet emphasis is on export industries. Those firms that are already dealing with the Soviet Union may see a Soviet presence through joint venture enterprises further cementing their relationship with the Soviet market. Although Soviet wages will not prove to be as low as those in many East Asian lands (e.g., Philippines or Thailand), the anticipated lower price of labor also will be attractive.

In summary, while there likely will be advantageous investment opportunities in the Soviet Union, prospective western investors will be well advised to proceed with caution. Although there may be early opportu-

nities in selected areas, such as services and tourism, it is likely that other Eastern bloc countries will find the investment climate under the Soviet joint venture law more palatable, at least initially, than will Westerners. For the immediate future, the significance of the Soviet joint venture law likely will be more political than economic in nature. In the long run, however, the Soviets would be well advised to reflect on the growing evidence that it is the general political and economic environment, more than temporary economic incentives, that draws foreign investors.¹⁵¹

VI. THE TRADE DIMENSION

This section will analyze the trade dimension of United States foreign economic policy towards the communist world, with emphasis on the Soviet Union. Particular attention will be given to those differences in the Western and Soviet systems which pose barriers to a more meaningful economic engagement through trade, and to the conflicting goals of the two systems which somehow must be accommodated as trade relations are developed.

The Sino-United States experience since the 1979 trade agreement has clearly demonstrated that successful East-West economic relations can be developed. According to United States figures, trade between the two countries reached \$10 billion in 1987, an increase of 20% over 1986.¹⁵² The increase of textiles exports, one of China's most important export commodities to the United States, has grown at an annual average rate of 45% since 1980.¹⁵³ In February, 1988, the two countries signed a four year textile agreement that further regularized the relationship.¹⁵⁴ China's trade with its former political nemesis, Taiwan, (and the United States ally which provided the sticking point in normalization of Sino-United States relations for many years) now conduct substantial indirect trade relations through Hong Kong.¹⁵⁵ Although the Sino-United States

¹⁵¹ *Developing Nations Urged to Ease Investment Rules*, Asian Wall St. J., Jan. 26, 1988, at 17, col. 1.

¹⁵² *Yeutter Expected to Urge China to Open Markets Wider to U.S.*, Asian Wall St. J., Feb. 1, 1988, at 1, col. 4. Figures released by the United States show a U.S. trade deficit in the relationship, but figures released by China claim a Chinese trade deficit. (China does not include its exports to the U.S. through Hong Kong.) *See Level of Trade Rises Between U.S., China*, Asian Wall St. J., Jan 28, 1988, at 33, col. 1. *See also Expected Rise in Trade With U.S. Underlines China's Growing Role*, Asian Wall St. J., Dec. 18-19, 1987, at 5, col. 4.

¹⁵³ *China, U.S. Starting Talks in Washington on Textile Imports*, Asian Wall St. J., Dec. 8, 1987, at 12, col. 6.

¹⁵⁴ *China and U.S. Sign Textile Agreement That Limits Exports*, Asian Wall St. J., Feb. 3, 1988, at 3, col. 1.

¹⁵⁵ During 1987, China-Taiwan trade (via Hong Kong) reached \$1.51 billion, up 58.7% from 1986. *China, Taiwan Trade*, Asian Wall St. J., Feb. 26-27, 1988, at 8, col. 2. *See also, Taiwan China Trade Seen Surging to Record in Year*, Asian Wall St. J., Dec. 14, 1987, at 5, col. 1.

trade relationship is not without problems, the relationship has regularized and contributed to vastly improved East-West relations. Some of the problems that do exist are no different than problems encountered in recent years by the United States in its trade relations with many long standing capitalist allies. Other problems may be attributed, at least in part, to the difference in approaches between the communist East and capitalist West.

A. Protectionism

The high level of protectionism in both China and the Soviet Union is a problem must be addressed if trade relations are to become more fully developed. This problem is particularly acute in the Soviet Union, where protectionism is institutionalized. Lenin's foreign economic policy was extremely protectionist, and has been carried out in the Soviet Union not so much by a traditional tariff approach but by a total government monopoly on foreign trade. The self-imposed isolationism of the Soviet Union was used to limit contact with the influence of Westernization. So long as the Soviets were willing to conduct trade in a relatively isolated posture, focusing trade relations primarily on members of the Council for Mutual Economic Assistance ("COMECON")¹⁵⁶ members and other communist countries, it could afford to maintain its extreme protectionist views towards the non-communist world. The result was that the Soviet Union has been left behind as other nations, including other communist nations such as China, have begun an aggressive modernization effort.

There appeared to be an increased Soviet interest in broader based international trade during the 1960s and 1970s, but this was primarily evidenced by the fact that there were increases in energy and gold prices, its principal exports. It was not until the late 1980s that the Soviet Union's leadership began to suggest that it was important to become involved in foreign competitive markets. Protectionism now stands as a substantial barrier to that involvement.

B. Match of Market and Plan

A continuing problem in trade relations will be the uneasy match of free market economies and planned economies. One of the most significant threshold questions in the negotiation of trade agreements between the United States capitalist market economy and the socialist non-market

¹⁵⁶ The Council for Mutual Economic Assistance was founded in 1949 in response to the organization of Western Europe under the U.S. Marshall Plan. Today it roughly serves as the Soviet bloc counterpart to the European Economic Community. See generally, T. HOYA, EAST-WEST TRADE 9-23 (1984).

economies is the role of government in making promises and providing assurances of compliance. Under the market economy model, government assumes more of a bystander role while private sector traders negotiate contractual terms on such matters as goods and currency for exchange, volume and timing of trade, and duration of trade relations. The private parties also have freedom to select forums for adjudication of disputes (e.g., arbitration) and to provide other assurances of compliance (e.g., letters of credit). Typically, the role of the state is limited to providing only the general framework (e.g., customs, tariffs) for transit of goods across borders, and leaving negotiation of transactional details to the private parties. Under the traditional version of the centrally planned non-market economy, the state controls all sectors involved in trade, and state agencies are directly responsible for the negotiation of detailed terms of trade and for assurances thereon.

In part because of the greater bargaining power of the United States, it has been able to secure trade agreements with communist nations that have more or less followed the market economy model.¹⁵⁷ There have been some significant exceptions, such as the United States-Soviet grain agreements¹⁵⁸ and maritime agreements,¹⁵⁹ in which each of the signatory states exchanged promises and assurances, as principal contractors, on such matters as commodity description, price, level of supply, duration of trade, and other details of the bargain.

Significant decentralization of foreign trade controls has occurred in China during the past decade. The promises of increased decentralization and introduction of more market-oriented business approaches in the Soviet Union suggest that it too will evolve towards more limited state involvement in the determination of business details, although there is nothing yet to suggest the extent of decentralization that has occurred in China.

¹⁵⁷ Agreement between the Government of the United States of America and the Government of the Union of Soviet Socialist Republics Regarding Trade, Oct. 18, 1972, 67 Department of State Bulletin 595 (1972), Bureau of East-West Trade, U.S. Department of Commerce, U.S./Soviet Commercial Agreements 1972, at 88 (1973), 11 I.L.M. 1321 (1972); Agreement on Trade Relations Between the United States of America and the Socialist Republic of Romania, April 2, 1975, 26 U.S.T. 2305, T.I.A.S. No. 8159; Agreement on Trade Relations Between the United States of America and the Hungarian People's Republic, March 17, 1978, 29 U.S.T. 2711, T.I.A.S. No. 8967. Sino-U.S. Trade Agreement, *supra* note 30. For a commentary on the differences of the two approaches, see T. HOYA, *supra*, note 156, at 9-23.

¹⁵⁸ *E.g.*, Agreement between the Government of the United States of America and the Government of the Union of Soviet Socialist Republics on the Supply of Grain, Oct. 20, 1975, 26 U.S.T. 2971, T.I.A.S. No. 8206.

¹⁵⁹ *E.g.*, Agreement between the Government of the United States of America and the Government of the Union of Soviet Socialist Republics Regarding Certain Maritime Matters, Oct. 14, 1972, 23 U.S.T. 3573, T.I.A.S. No. 7513.

C. Admission to GATT

The goal of the General Agreement on Tariffs and Trade (GATT) is to reduce tariffs and other trade barriers in order to liberalize world trade.¹⁶⁰ Because the Soviet Union is not a member of GATT, it does not enjoy most-favored-nation status and the Agreement's protections from discriminatory tariffs.¹⁶¹ In 1973, the United States Commerce Department proposed that the Soviet Union join GATT, but it declined. In 1982 and 1986 it expressed its desire to join, but was rejected by GATT's largely Western membership.¹⁶²

The difficulty of meshing market and plan was highlighted when the Soviet Union applied for admission to GATT in 1986, but was quickly rebuffed by GATT's market economy membership.¹⁶³ The Soviet Union has outlined an ambitious agenda for changes in its foreign trade policy, and membership in GATT is a major objective.¹⁶⁴ The objections from the United States when the Soviets attempted to join GATT, on the eve of the November 1986 Punta del Este meeting of the Uruguay Round of GATT negotiations, were focused principally on the lack of a free market economy.¹⁶⁵ Specific impediments include the high level of Soviet subsidies to domestic industry engaged in export trade and pervasive protectionist barriers against imports. Under *perestroika*, the Soviets are attempting to address that challenge. Unless the Soviet Union drastically modifies its posture towards the United States and its interests, it would be risky at best to permit the Soviet Union to join IMF or GATT. The Soviet Union would thereby gain not only access to more favorable trade relations with our trading partners, but also significant new fora for anti-United States actions and rhetoric.

China, which has enjoyed most-favored-nation treatment by the United States since 1979, stands a better chance for admission to GATT.¹⁶⁶ In the meantime, however, China has complained about the

¹⁶⁰ General Agreement on Tariffs and Trade, *opened for signature* Oct. 30, 1947, 61 Stat. A3, T.I.A.S. No. 1700, 55 U.N.T.S. 187, 188 (effective Jan. 1, 1948)[hereinafter GATT].

¹⁶¹ *Id.*, art. I (Most Favored Nation Clause). See *Soviets Play the Alphabet: EC, Now GATT, Next INF?*, BUS. EASTERN EUROPE, Sept. 8, 1986, at 284; Klingenberg & Pattison, *Soviet Announcement Should Stir Interest of U.S. Corporations*, Legal Times, Mar. 2, 1987, at 13, col. 1.

¹⁶² J. HOUGH, *supra* note 53, at 57.

¹⁶³ The opposition was led by the United States when GATT membership was denied. *U.S. to End its Soviet Nickel Ban*, N.Y. Times, Dec. 6, 1986, at 40, col. 4. The U.S. opposition has continued into 1988. *Soviet Union: Stance on Soviet Membership in International Economic Organizations Unchanged, U.S. Says*, 5 Int'l Trade Rep. (BNA) 116 (Jan. 27, 1988).

¹⁶⁴ *Soviet Official Outlines Ambitious Policy Charges Sought in Foreign Trade Agenda*, 5 Int'l Trade Rep. (BNA) 151 (Feb. 3, 1988).

¹⁶⁵ *Id.*

¹⁶⁶ Both the Soviet Union and China are pressing for changes that will place their application to

United States unwillingness to give China Generalized System of Preferences treatment pending approval of its GATT petition. China argues that it should be extended this preferential treatment because most of its trade already is with GATT member nations.¹⁶⁷ In response, the United States government continues to express its concerns about China's protectionist policies, which generally are carried out by very high tariffs.

D. Technology

One of the major sticking points in East-West trade will continue to be the demand in communist countries for the West's advanced technology. Both China and the Soviet Union have been particularly critical of United States limitations on exports of technology; the need for technology is a principal motivation for their opening to foreign joint ventures.¹⁶⁸ Although the Soviet Union contends that it is sufficiently advanced to be a world competitor in high technology, the United States continues to hold its lead in technology.¹⁶⁹ With its new modernization programs, the Soviet Union has an even greater need for the infusion of industrial technology. Too often, advanced industrial technology has significant military applications. So long as it is perceived as a military risk to the free world, however, it will remain the target of United States technology export controls.

The United States trade controls for national security purposes are found principally in the Export Administration Act (EAA) of 1979, as amended in 1985.¹⁷⁰ This complex legislation vests considerable discretion in the executive branch, and was intended to be used sparingly so as to minimize harm to United States business while protecting national

GATT in a more favorable light. See, e.g., *Beijing Assures GATT it Will Speed Reform*, Asian Wall St. J., Feb. 24, 1988, at 3, col. 2; *Soviet Planners Push for Subsidy Cut*, Asian Wall St. J., Dec. 10, 1987, at 20, col. 4.

¹⁶⁷ *China Unlikely to Satisfy the U.S.*, Asian Wall St. J., Feb. 1, 1988, at 1, 8, col. 5.

¹⁶⁸ See, e.g., the Chinese Joint Venture Law, *supra* note 35, art. 5:

The technology and equipment contributed by a foreign joint venturer as its investment in kind must be advanced technology and equipment that really suits China's needs. In case of losses caused by a foreign joint venturer practicing deception through the intentional provision of outdated technology and equipment, it shall compensate for the losses.

¹⁶⁹ The Reagan Administration has made it clear that improved U.S.-Soviet relations is no reason for relaxation of COCOM export controls. *Current Thaw in Relations with Soviets is no Reason to Weaken COCOM*, *Wendt Says*, 5 Int'l Trade Rep. 1003 (July 13, 1988).

¹⁷⁰ 50 U.S.C.A. App. §§ 2401-2420 (1982 & Supp. III 1985). The goal of this legislation is to restrict the export of goods and technology "which would make a significant contribution to the military potential of any other country or combination of countries which would prove detrimental to the national security of the United States; and are necessary to further significantly the foreign policy of the U.S. or to fulfill its declared international obligations." § 2401. This goal is accomplished through export controls consistent with specific criteria established by Congress. See 1982 *Hearings*, *supra* note 31, at 196 (statement of Alexander B. Trowbridge).

interests. The President is authorized to "prohibit the exportation of any articles subject to the jurisdiction of the U.S. or exported by any persons subject to the jurisdiction of the U.S."¹⁷¹ The President's authority is delegated to the Department of Commerce. The most effective restraint is found in the licensing requirements. The licensing requirement may be used to totally bar exports to certain communist nations,¹⁷² while permitting relatively more liberal issuance of export licenses for shipments destined to other communist trading partners, such as China.

The EAA is a very effective tool when properly used. Until the Soviet Union demonstrates through more tangible actions the sincerity of its desire not only to do business with the United States, but also to normalize relations in non-economic arenas as well, the EAA will remain a major barrier to technology exports to the USSR.

E. Fiscal and Monetary Reforms

In addition to GATT membership, another major Soviet objective is to establish a convertible ruble.¹⁷³ This objective is intimately linked to the first, as convertibility requires that Soviet prices be free to reflect world prices. That ultimately will call for abolition of centralized allocation of resources in favor of a market-oriented economy.¹⁷⁴

Some tentative, but important, steps are already being taken. In March, 1988, for example, the Soviet Union and Czechoslovakia agreed to use national currencies in settling commercial accounts between Soviet and Czech enterprises engaged in joint ventures for production or for technological or scientific development.¹⁷⁵ This was the first agreement of its kind among members of COMECON. Similar agreements are expected between the Soviet Union and other Eastern bloc countries.¹⁷⁶

The Eastern bloc posture on credit and monetary relations in general has been changing significantly. In recent years, reduction in revenues from the principal Soviet exports of oil and gas has resulted in increased pressures on the available pool of hard currency. Other nations in the ten-nation COMECON trade block are having similar diffi-

¹⁷¹ 50 U.S.C. App. § 2402 (1982 & Supp. III 1985).

¹⁷² E.g., virtually all applications for export licenses to North Korea, Kampuchea, Vietnam and Cuba currently are being denied. 15 C.F.R. § 385.1 (1988).

¹⁷³ *Soviet Official Outlines Ambitious Policy Changes Sought in Foreign Trade Agenda*, 5 Int'l Trade Rep. (BNA) 151 (Feb. 3, 1988) [hereinafter *Soviet Official Outlines*]. See also, *Soviets Seek Convertible Rouble*, Asian Wall St. J., Feb. 4, 1988, at 10, col. 5.

¹⁷⁴ *Ruble Reform Trade-Offs Test Soviet Ideology, Bureaucracy*, Asian Wall St. J., Mar. 1, 1988, at 1, col. 1.

¹⁷⁵ *Czechoslovakia, Soviet Union Embark on Plan Intended to Lead to Currency Convertibility*, 5 Int'l Trade Rep. (BNA) 333 (Mar. 3, 1988).

¹⁷⁶ *Id.*

culties. As a result, total East bloc borrowing during the past three years increased 55% to a total of almost \$127 billion dollars. This is a greater indebtedness than that of Brazil or Mexico.¹⁷⁷ With most of the Third World countries awash in debt, capital-rich western banks (particularly those in Japan and Europe) are providing credit to the Soviet Union at the rate of \$700 million dollars a month. Most of the loans are free to be spent by the Soviets as they please.¹⁷⁸

In China, the progress of economic reforms are affecting both the investment and monetary systems of the nation. Traditionally, allotment of investment capital was exclusively within the province of the central monolithic administrative structure. Pluralistic investment sources have arisen, and there now are increasing pressures to transfer substantial portions of the nation's investment decision making power to enterprises. Such a change would also require a more efficient monetary system, with financial agencies specializing in investment.¹⁷⁹

China has joined the Soviet Union in the international credit market as a borrower. It is expected that China will remain a major borrower of foreign capital until at least the year 2050.¹⁸⁰ While loan demands from other members have been stagnant in 1987, China became one of the two largest borrowers from the Asian Development Bank, along with India.¹⁸¹ The role of China and the Soviet Union as borrowers will increase the need for more openness on their financial dealings.

The Soviet Union also has entered international credit markets in the role of lender; negotiations by a West German concern for a \$355.8 million construction project loan from the Soviet Bank of Foreign Affairs was announced in early 1988.¹⁸²

F. Increased Economic Relations with Western Europe and Developing Nations

The third major objective of the Soviet Union is to strike a mutually beneficial trade agreement with the EEC. The Soviets reportedly are seeking "the widest possible and most complete agreement" they can get with the EEC, covering major sectors of the economy and guaranteeing

¹⁷⁷ *Gorbachev Courts Capitalism, but Only Abroad*, Asian Wall St. J., Dec. 19, 1987, at 10, col. 3.

¹⁷⁸ *New Soviet Role as Bond Issuer Requires Glasnost*, Asian Wall St. J., Jan. 8 9, 1988, at 9, col. 3.

¹⁷⁹ See *China Needs New Investment System*, China Daily, Oct. 7, 1987, at 4, col. 1. Similar reforms may lie in the future for the Soviet Union.

¹⁸⁰ *China to Remain Big Borrower*, Asian Wall St. J., Dec. 18-19, 1987, at 17, col. 1.

¹⁸¹ *China and India Lift ADB Loans to a Record*, Asian Wall St. J., Jan. 29 30, 1988, at 1, col. 6.

¹⁸² *Soviets Entering Credit Markets in Role of Lender, not Borrower*, Asian Wall St. J., Jan. 19, 1988, at 20, col. 1.

freer trade with the Soviet Union.¹⁸³ It is significant that the joint venture law already has attracted substantial West European investment. By late 1987, fully one half of the joint venture agreements signed under the new law were with West German companies.¹⁸⁴

At a time when the United States appears unable to develop a coherent and sustained policy for dealing with developing nations, Moscow has increased its attention and focus on key developing areas of the world. Those areas are of critical importance not only because of their potential for future development, but also because they provide many of the raw materials needed by the West, and often are strategically located as well.¹⁸⁵

G. Soviet Economic Agencies Restructured

To their credit, the Soviets have instituted major internal organizational changes at the policy making level in order to carry out the new Soviet policies of encouraging increased international trade and investment. The Foreign Economic Commission of the Council of Ministers has been formally established as the coordinator of foreign economic policy. The Ministry of Foreign Affairs has established a formal Department of Foreign Economic Administration to coordinate efforts in dealing with international organizations such as the International Monetary Fund and the World Bank.¹⁸⁶ The State Committee on Foreign Economic Ties also has received increased authority, and has been given the right to serve as the general contractor for foreign construction inside the Soviet Union. Apparently, it will be the agency primarily responsible for the construction of joint ventures under the new foreign joint venture law.¹⁸⁷ There also are indications that the Ministry of Foreign Trade will no longer enjoy its exclusive monopoly power over trade relations with other countries.¹⁸⁸

Soviet foreign trade organizations function as middlemen for Soviet foreign trade transactions, and act on behalf of and sign contracts for the Soviet party.¹⁸⁹ In the past, each foreign trade organization has enjoyed a monopoly over the import and export of a specific type of goods.¹⁹⁰ This monopoly has been substantially broken as a result of Gorbachev's

¹⁸³ *Soviet Official Outlines*, *supra* note 173, at 151.

¹⁸⁴ Brady, Galuszka, & Lewald, *supra* note 113, at 154.

¹⁸⁵ *Soviets Let Off Hook*, *Asian Wall St. J.*, Dec. 10, 1987, at 12, col. 4.

¹⁸⁶ *Id.*

¹⁸⁷ *Id.*

¹⁸⁸ J. HOUGH, *supra* note 53, at 61-64.

¹⁸⁹ T. HOYA, *supra* note 156, at 285-86.

¹⁹⁰ *Id.* at 11-12.

economic reforms.¹⁹¹ On January 1, 1987, twenty-one ministries and sixty-eight enterprises were given trading rights which permit them to deal directly with foreign companies.¹⁹² Only the export of fuels and raw materials will continue to be controlled exclusively by the Ministry of Foreign Trade.¹⁹³

This decentralization of trading rights will make more Soviet entities available for joint venture purchases and sales in the Soviet market, and for trade with foreign companies and governments abroad. However, some initial problems are bound to surface from this new development. Because foreign trade organization officials are the only Soviets with knowledge and experience concerning foreign trade, many of them likely will be transferred to one of the industrial ministries or enterprises recently granted trading rights.¹⁹⁴ A United States company with experience in the Soviet market may have difficulty locating its previous contracts due to such transfers. Thus, even though a United States company or joint venture may have more freedom to buy and sell in the Soviet market, it may have considerable difficulty in locating the correct official or organization to conduct its business. As a result, some observers have predicted that this reorganization of foreign trade probably will result in chaos,¹⁹⁵ and that it may take years to establish the reorganization and restore prior contacts.¹⁹⁶

Moreover, if the United States company decides to deal directly with a ministry or enterprise with trading rights, the process may proceed slowly and prove to be frustrating and unproductive. Soviet trade and industrial officials need education in Western business principles.¹⁹⁷ Many of them have little or no experience with foreign trade. Particularly with respect to trade with joint ventures, they are proceeding cautiously because they want the first joint ventures to be profitable.¹⁹⁸

Finally, the huge Soviet bureaucracy is having difficulty adjusting to the new economic reform.¹⁹⁹ Some foreign ventures in the Soviet Union have been abandoned in the face of rivalry, turf protection, and lack of coordination among the ministries.²⁰⁰ Rank Xerox's experience with two

¹⁹¹ Gumbel, *Moscow Enigma: Soviet Plan to Let in Foreign Firms Proves Frustrating in Practice*, Wall St. J., July 17, 1987, at 1, col. 1.

¹⁹² *Soviet Foreign Trade Shakeup Confirmed*, BUS. E. EUR., Sept. 15, 1986, at 289.

¹⁹³ *Id.* at 289.

¹⁹⁴ *Soviet Foreign Trade Shakeup Confirmed*, *supra* note 192, at 290.

¹⁹⁵ *Soviet Trade Reform: Change, with Confusion*, BUS. E. EUR., Feb. 23, 1987, at 58.

¹⁹⁶ Zabijaka, *supra* note 99, at 9.

¹⁹⁷ Gumbel, *supra* note 191, at 1, col. 1.

¹⁹⁸ Brady, Galuszka, *supra* note 103, at 77-78.

¹⁹⁹ Gumbel, *supra* note 191, at 1, col. 1.

²⁰⁰ *Id.* at 1, col. 1 and at 9, col. 3.

Soviet ministries provides a good example. Because the ministry producing paper for export and the one importing and assembling the copy machines could not coordinate their efforts, Rank Xerox's original venture could not be finalized.²⁰¹ A major Western chemical company had a similar experience when it proposed to manufacture a herbicide presently imported by the Soviets. The Chemical Industry Ministry would not commit the raw materials and the Ministry of Agriculture would not agree to purchase the end product from the Fertilizer Ministry slated to produce the herbicide.²⁰²

Clearly, there is a great need for further reform if the Soviet Union is to be integrated into the Western trading system. However, reforms that have been made to date are encouraging. Even if these reforms are successful and trade and investment policies are further liberalized, a major obstacle to normalization of economic relations between the United States and the Soviet Union is the Soviet record on human rights. That dimension of the problem, which was highlighted by President Reagan during the May-June 1988 United States-Soviet Summit meeting in Moscow,²⁰³ must be addressed and resolved as an integral part of any new economic policy towards the East.

VII. THE HUMAN RIGHTS DIMENSION

A. Glasnost and the "Democratization" Movement

The reforms in China and the Soviet Union hold potential for far greater changes in those societies than mere rehabilitation of the national economies. Political reforms have been promised and are badly needed. Political and economic corruption has become a serious problem in both countries, and economic reform cannot take place without political reform. Tentative but important steps already have been taken, but resistance is deeply rooted in self-interested and privileged bureaucracies.

Whether the Party will in fact surrender any substantial part of its powers, as has been promised in China, is yet to be seen. The promise is yet to be made in the Soviet Union. However, one long term effect of economic reforms may be an increased demand, if not satisfaction, of the democratic instincts of the masses.

Gorbachev has promised *glasnost* in Soviet society, pledging more openness in the workings of his traditionally hyper-secretive government.

²⁰¹ *Id.* at 9, col. 3.

²⁰² *Id.*

²⁰³ Church, *A Gentle Battle of Images: Behind All the Ceremony was a More Subtle Form of Posturing*, TIME, June 13, 1988, at 21-22.

Both the Soviets and Chinese governments have spoken increasingly of "democracy," but one fact should be abundantly clear: neither the Soviet nor Chinese communist definitions of "democracy" are similar to that concept as understood in the United States. *Democracy* in the traditional sense of that word meant direct governance by the people. Since direct governance is impossible in a large modern state such as the United States, China, or the Soviet Union, the best that can be hoped for is meaningful participation in and influence upon the government through representatives of the people, *i.e.*, a democratic republic.²⁰⁴

It is that meaningful participation by the people, through voting and numerous other measures, that structurally distinguishes the United States political system from the systems in the communist states. In the case of China, the distinction is as much cultural as it is political. We accept as part of our democratic philosophy that individuals and groups may pursue their own selfish interests with the state, not only through voting, but through lobbying efforts, publicity campaigns, and other means that draw heavily on the fundamental Constitutional rights of free expression, free press, and freedom of association. The right to challenge government, and in fact to place oneself in an antagonistic posture versus government, we take as given rights.²⁰⁵ These rights are in turn protected and preserved by an independent judiciary that ensures that the rule of law prevails over the rule of man.

The Leninist view on these matters is clear, and such antagonistic postures against the state simply will not be tolerated. Law is nothing more than a tool of the state to ensure its supremacy. Communist theory holds that the state always knows what is best for the people and therefore, by definition, anyone opposing the state is opposing the best interest of the people. A neater fiction could not be devised to preserve power for a ruling elite.

In China, centuries of tradition built upon ancient philosophies stressing harmony among the individual, family and state continue to have their impact today. What may appear to be a facile identification of the people's interest with the interest of the ruling elite (who act in the

²⁰⁴ See D. SPITZ, PATTERNS OF ANTI-DEMOCRATIC THOUGHT 8-9 (1965).

²⁰⁵ Although the right to speak out has not been taken for granted in China, there have been some recent cases of unprecedented tolerance. Fang Lizhi, a prominent Chinese astrophysicist, has been particularly and openly critical of both the Chinese government and Party, and has denounced socialism in general. He was blamed for inciting students during the January 1987 student rights demonstrations, and lost both his Party membership and post as university vice president. Although he reportedly is closely watched, he has been allowed to socialize and go about his academic life with surprising freedom. Schell, *China's Andrei Sakharov*, THE ATLANTIC MONTHLY, May 1988, 35, 151.

name of the state), nevertheless is consistent with the traditional Chinese philosophy that rulers and ruled have an essential harmony of interests. For that reason, the Chinese were culturally susceptible to the introduction of communist theory.

However, as the Chinese people begin to enjoy the taste of a better life as a result of economic reform, have increased exposure to the outside world, and thereby gain a heightened awareness of the alternatives to communism, their demands for more democracy in the Western sense ineluctably will increase. The same phenomenon no doubt will appear in the Soviet Union as well, if the reforms proceed as promised. When those demands are considered too strident, threatening or embarrassing for the ruling elite, non-democratic responses will follow, as they did in the aftermath of Beijing's 1987 student protests. But such authoritarian responses will become less defensible in the face of continued rhetoric on "democracy," coupled with a broadening application of the rule of law.²⁰⁶

The regime of Deng Xiaoping has taken historic though tentative steps towards greater democratization in China. A sustained effort has been made throughout most of the past decade to establish the rule of law, a concept so essential to democracy, but virtually alien to China under Mao Zedong. China is now engaged in the task of popularizing legal knowledge, which is viewed as a key in the nation's current reform efforts.²⁰⁷ As a nation of people historically under some form of imperial rule by one or a few of the favored elite, a principal obstacle now facing Beijing is to educate the populace and gain acceptance of the rule of law outside the nation's capital. Beijing's lawmakers appear to understand the significance of law in lieu of despotism, not only its role in attracting western trade and investment, but also its role in the enhancement of a sense of security and well being among the people. But the heavy layer of bureaucrats standing between the people and the capital appear yet to be fully convinced.

In the Soviet Union, Gorbachev has recognized that new legislation can serve as a principal pillar upon which his restructuring of society can

²⁰⁶ During early 1988, Gorbachev was faced with major disturbances by Armenians who engaged in national protests challenging Moscow's leadership. The demonstrations centered on demands that the Nagorno-Karabakh Autonomous Region be incorporated into Armenia. The protests have made Gorbachev vulnerable to his critics who claim that his new reform measures will breed disorder. See *Soviet Leader Appeals to Armenians to End Protest*, St. Petersburg Times, Feb. 27, 1988, at 12A, col. 1. In recent years, there have been other demonstrations by various nationality groups seeking more autonomy, including the Kazakhs in Soviet Central Asia, and Latvians, Lithuanians and Estonians in the Baltic Republics.

²⁰⁷ *Reforms Require Legal Knowledge*, China Daily, Oct. 13, 1987, at 4, col. 1.

be founded.²⁰⁸ When he speaks of democratization, he typically speaks in guarded terms of a form of "economic democratization" in the workplace.²⁰⁹ But he appears to recognize that law is an indispensable element in that democratization process.²¹⁰

If *perestroika* does have its desired economic impact, including increased trade and investment from the West, and if *glasnost* does result in greater openness to domestic and international scrutiny of the Soviet State's relationship with its people, then Gorbachev's theories of democratization will be put to a rigorous test in the coming decade. For no matter what subtle shades of meaning may attach to democratization under socialist legality, the West will judge progress largely in terms of basic human rights.

B. The Human Rights-Trade Linkage and Economic Sanctions

The techniques by which the United States has manifested its human rights concerns in the past, however, have not been very successful with its principal target, the Soviet Union. The United States policy articulated in the Jackson-Vanik amendment to the 1974 Trade Act²¹¹ conditions most-favored-nation status for the Soviet Union on its emigration performance. The Soviets perceive this condition as an affront to their sovereignty, and as an attempt by the United States to impose its policies extraterritorially in areas of Soviet domestic concerns.

Many observers believe that the United States policy embodied in the Jackson-Vanik amendment has been, on balance, counterproductive.²¹² There is no evidence that the Jackson-Vanik amendment itself has been a significant factor in altering Soviet emigration policies.²¹³ One scholar recently argued that:

²⁰⁸ M. GORBACHEV, *supra* note 14, at 107.

²⁰⁹ See, e.g., *id.* at 102-05.

²¹⁰ "There can be no observance of law without democracy. At the same time, democracy cannot exist and develop without the rule of law, because law is designed to protect society from abuses of power and guarantee citizens and their organizations and work collectives their rights and freedoms." *Id.* at 105.

²¹¹ Trade Act of 1974, Pub. L. No. 93-618, § 402, 88 Stat. 2056 (1975)(codified at 19 U.S.C. § 2432 (1982)).

²¹² For example, the Atlantic Council of the United States recommended on April 1, 1987 that most-favored-nation treatment be extended to the Soviet Union. The Council argues that most favored nation status primarily should be an economic consideration, because conditioning such status on Soviet emigration policies neither increases emigration, nor does it improve U.S.-Soviet relations. *The Soviet Union Should be Granted Most Favored Nation Status*, 4 Int'l Trade Rep. (BNA) 458 (Apr. 1, 1987).

²¹³ See comments of United States Commerce Secretary, C. William Verity, *Administration Does Not Plan to Address Jackson-Vanik Waiver at Summit*, Verity Says, 5 Int'l Trade Rep. (BNA) 691 (May 11, 1988).

In the age of Soviet *glasnost* and economic reform, it is anachronistic to treat the formal right of emigration as the only human right worth defending It is hard to justify the construction of [economic] barriers to this process without a compelling military reason; it is bizarre to do so in the name of human rights or to be more specific, one human right.²¹⁴

As has been proven by the Soviet experiences, economic sanctions are not likely to be effective in dealing with a large, powerful, and relatively self-sufficient nation, particularly when it has wide access to alternative sources to supply its needs. In the contemporary world of shifting and multilateral alliances, sanctions are difficult to enforce and are frequently criticized as ineffective.²¹⁵ What has happened in the face of United States sanctions in the past, and is likely to happen in the future, is that the Soviet Union simply will turn to other suppliers, including some of our allies. In order for economic sanctions by the United States to be effective, we need cooperation from other countries that might provide those alternative sources, along with clearly articulated objectives, and pressure applied to a vulnerable point of dependency of the target nation. To be most effective, the sanctions must be selective and infrequently imposed.²¹⁶ For those reasons, the sanctions based on trade controls tend to work most effectively against the most vulnerable targets, i.e., smaller and less defensible economies which can be isolated from other nations, and which will suffer greatly from such isolation. Given all of the above circumstances, it is easy to see why economic sanctions by the United States against the Soviet Union have only a spotty track record for success.²¹⁷

Another problem with United States economic sanctions is that they give the target nation an external excuse for its failures, namely the United States. Examples are abundant, but to list only a few, the rulers of Cuba, Nicaragua, Poland and others have continued repressive policies in the face of United States sanctions, and the sanctions themselves have become as much the focal point of public animosity as have the oppressive regimes' own policies.²¹⁸

Some of the losses occasioned by the United States when economic sanctions are imposed, particularly when they are ineffective, include di-

²¹⁴ J. HOUGH, *supra* note 53, at 96. However, there is considerable support for the contrary view. For example, the Conservative Caucus has called for application of a modified version of the Sullivan Principles developed for labor practices in South Africa to United States firms operating in the Soviet Union and other communist countries. *Sullivan Principles for Firms in Soviet Union are Advocated by Conservative Caucus*, 5 Int'l Trade Rep. (BNA) 723 (May 18, 1988).

²¹⁵ See, e.g., Stevenson, *Toward a More Rational East-West Trade Policy*, 1983 J. LEGIS. 11, 25.

²¹⁶ Doxey, *Economic Sanctions: Benefits and Cost*, 36 WORLD TODAY 484, 485-86 (1980).

²¹⁷ Miller, *When Sanctions Worked*, 1980 FOREIGN POL. 118, 126 (Summer).

²¹⁸ J. HOUGH, *supra* note 53, at 97.

rect financial costs, the loss of favorable economic transactions, damaged business relations with not only the target country but with allies who choose to do business with it in spite of the sanctions, and the long term loss of market share by United States businesses. Non-economic costs include increased international tension, domestic political tensions, and ultimately, diminished utility of sanctions because of the frequency of their use.²¹⁹ This is not to suggest that sanctions should never be used against a country like the Soviet Union, but they should be used sparingly, and with full recognition of their limited utility.

The inconsistent application of the Jackson-Vanik linkage of United States most-favored-nation treatment to emigration policies is exemplified in the case of the People's Republic of China, and illustrates why economic engagement is preferable to economic isolation under the present circumstances. In 1979, the Sino-United States Trade Agreement extended MFN status to China. The restrictive emigration policies of China apparently were ignored because other foreign policy concerns received priority treatment, but also because of the practical consequences that would flow from an abrupt liberalization of Chinese emigration policy. If the United States had insisted on free emigration as a condition of granting most-favored-nation treatment to China, and China had conceded by liberalizing its emigration policies, the result could have been disaster for the United States. President Carter apparently was taken aback when Deng Xiaoping told him that, "If you want me to release ten million Chinese to come to the United States, I'd be glad to do so."²²⁰

Based upon Gorbachev's pronouncements regarding the new policies of *glasnost* and *perestroika*, there may be hope that the Soviet leadership will recognize the need for human rights reform regardless of any positions taken by the United States or other countries. At the very least, however, Gorbachev appears to have recognized the relationship between increased productivity and worker morale; an oppressed and demoralized people are not likely to give their best to achieve the state's production goals.

Western human rights critics of China have focused on a variety of concerns, including certain aspects of China's population policy, restraints on freedom of expression, and suppression of the freedom of religion. In September 1987, the Dalai Lama, Tibet's God-King in exile,

²¹⁹ Rosenthal, *The Soviet Pipeline and Its Legal Implications for United States Foreign Policy*, 2 FLA. INT'L L.J. 27, 48-49 (1986).

²²⁰ J. CARTER, KEEPING FAITH: MEMOIRS OF A PRESIDENT 209 (1982). In contrast to China, the United States can afford to insist upon an open emigration policy in the Soviet Union because the United States shores are not likely to be threatened with hordes of Soviet emigres seeking entry into the United States.

made an unusual appearance before the United States Congress to present his call for Tibetan independence from China. Seizing the occasion of focused publicity, Tibetan separatists also staged riots on September 27th and October 1st to protest China's sovereignty.²²¹ The Dalai Lama's claim that more than one million Tibetans had been massacred by Chinese authorities, although unsubstantiated, was not only sensationalized by some members of the world press,²²² but also was cited by Congress in adopting companion resolutions condemning China for human rights abuses in Tibet specifically,²²³ and in China generally.²²⁴ However, the basic thrust of these companion resolutions was directed to abuses that occurred more than fifteen years earlier, during the cultural revolution led by the now-discredited regime of Mao Zedong.

The heinous crimes and abuses that were perpetrated during the cultural revolution not only had been chronicled by Amnesty International years earlier,²²⁵ but had been admitted and vilified by China's current leaders. One of the reasons that the abuses of the cultural revolution and the earlier abuses of the "anti-rightist" campaign had come to light in the first place was that they were openly exposed and denounced by members of Deng's new government.²²⁶ These were unprecedented steps by a regime that historically had been as secretive as the Soviet Union. In 1978, the United States State Department issued a public statement²²⁷ commending China's new leadership for exposing the past abuses to human rights in that country.²²⁸

²²¹ Anderson, *Bad Faith at the Temple*, NEWSWEEK, March 21, 1988, at 40; Ignatius, *Defiant Tibetan Claim Victory in Riots*, Asian Wall St. J., Oct. 6, 1987, at 1, col. 5.

²²² See, e.g., *Violence in Tibet*, Asian Wall St. J., Oct. 5, 1987, at 8, col. 1.

²²³ Foreign Relations Authorization Act, Fiscal Years 1988 and 1989, Pub. L. No. 101-204, § 1243, 101 Stat. 1331, 1422-24 (1987).

²²⁴ *Id.*, Pub. L. No. 101-204, § 1245, 101 Stat. 1331, 1425-26.

²²⁵ See AMNESTY INTERNATIONAL REPORT 1979; AMNESTY INTERNATIONAL REPORT 1980. See also R. EDWARDS, L. HENKIN & A. NATHAN, HUMAN RIGHTS IN CONTEMPORARY CHINA (1986).

²²⁶ Deng Xiaoping himself has been quoted as stating that nearly one million people died by mob action under the rule of the Gang of Four during the cultural revolution. See *Human Rights in Asia: Communist Countries: Hearings Before the Subcomm. on Asian and Pacific Affairs and on International Organizations of the House Committee on Foreign Affairs*, 96 Cong., 2d Sess., 44 (1980) (Statement of Charles W. Freeman). The Gang of Four consisted of a group of extreme leftists who ascended to power during Mao Zedong's waning years. They included Jiang Qing (Mao Zedong's wife), Zhang Chunqiao, Wang Hongwen, and Yao Wenyuan. Following Mao's death, all four were arrested. They were subjected to a public trial four years later and were found guilty of criminal acts. Two were given suspended death sentences, one a life term of imprisonment, and the fourth received a twenty year sentence. See generally, D. BONAVIA, VERDICT IN PEKING: THE TRIAL OF THE GANG OF FOUR (1984).

²²⁷ See *State Department Press Guidance*, 28 November 1978; *China Commended for Acknowledging Past Rights Abuses*, Washington Post, November 29, 1978, § A at 17, col. 1.

²²⁸ Although allegations have been made concerning political prisoners in China, very little relia-

If attention is focused on the more recent developments that are contemporary with the increasing economic relations between China and the West, a more encouraging view of China's human rights record develops. The so-called "democracy movement," which began contemporaneously with Deng Xiaoping's opening to the West, clearly had its impact.²²⁹ While it was suppressed in 1981, the new reformist government moved quickly to initiate the rule of law. Reforms soon enacted included greater freedom of travel by Chinese citizens, greater religious freedoms, a liberalization of restrictions on the economy, the release and rehabilitation of large numbers of political prisoners previously incarcerated, the admission of reformers into the party, and the allowance of greater local participation in government.²³⁰

On August 18, 1980, Deng Xiaoping made a major speech on reform of the Party and state leadership, in which he identified democracy as essential to China's modernization.²³¹ The new 1982 Constitution included a section on "Personal Rights," largely in response to the abuses endured by the Chinese people (and many of the leaders themselves, such as Deng Xiaoping) in the past.²³² Although there have been gaps be-

ble evidence exists that this is a widespread practice. See DEPARTMENT OF STATE, COUNTRY REPORTS ON HUMAN RIGHTS PRACTICES FOR 1979 at 440, 441 (1980). There have been some highly publicized cases, such as the fifteen year sentence given to Wei Jingshen, who was found guilty of providing "military secrets" to foreign correspondents. AMNESTY INTERNATIONAL REPORT 1980, *supra* note 224, 189-90. In 1981, China reportedly republished a 1951 law, entitled "Regulations on Guarding State Secrets," which prohibited Chinese from providing a wide range of information to foreigners. See, *Political Developments and Human Rights in the People's Republic of China: Hearings Before the Subcommittees on Human Rights and International Organizations and on Asian & Pacific Affairs of the House Committee on Foreign Affairs*, 99th Cong., 1st Sess., 67-68, 81, 266-67 (1985). However, in 1984, Amnesty International admitted that its own efforts had failed to gather complete information "concerning prisoners of conscience" in China. AMNESTY INTERNATIONAL REPORT 1984, 217-18.

²²⁹ From 1978 to 1980, the "democracy movement" in China was brought on by a spontaneous demonstration of the Chinese people of their desire for greater civil and political rights. In part, it no doubt was brought on by the relief occasioned by the anticipated end of the Mao Zedong era. The first indication that the movement was developing was when thousands assembled in Tiananmen Square on April 5, 1976, to mourn the death of Zhou Enlai and to protest the rule of the Gang of Four. By 1981, however, the party had decided to bring this movement under control, and unofficial publications, including posters on the "democracy wall" in Beijing, were banned. See A. NATHAN, CHINESE DEMOCRACY 10 (1985); F. BUTTERFIELD, CHINA: ALIVE IN THE BITTER SEA 411 (1982).

²³⁰ Cohen, *People's Republic of China: The Human Rights Exception*, 9 HUMAN RTS. Q. 447, 518 (1987).

²³¹ Deng stated that one of the three major objectives in China's modernization was:

to practice people's democracy to the full, ensuring that through various effective forms, all the people truly enjoy the right to manage state affairs and particularly state organs at the grass roots level and to run enterprises and institutions, and that they truly enjoy all the other rights of citizens.

Reform of System, *supra* note 142, at 4, col. 1.

²³² The 1982 Constitution provides:

[T]hat the personal dignity of citizens is inviolable; insulting, slandering, falsely charging or

tween reality and the paper promises of the Constitution and statutes, those gaps appear to have been closing with each passing year of Deng's government. Although the new legal codes in the early 1980s did not protect the "democracy movement" advocates from punishment, it appears they did result in a certain self-restraint.²³³ During the 1980s, China has increasingly become involved in the United Nation's efforts to ensure human rights, and has developed greater cooperation with Amnesty International and the international committee of the Red Cross.²³⁴

Traditionally, the United States has focused its international human rights concerns not only on the Soviet Union and other communist nations, but also on those countries which have a "special relationship" with the United States.²³⁵ China's increasing economic stake in its favorable relations with the United States, and the special economic relationship created thereby, clearly has had a favorable impact on the improvement of human rights in China.²³⁶

The Chinese experience over the past decade, while it may not meet all the human rights expectations of the United States, nevertheless provides a good argument for increased economic relations as a foundation for improved human rights conditions. As the nation's economic stakes are raised through international economic ties, international human rights norms will have greater influence. The economic isolationism and containment of the Soviet Union in the past has resulted in isolationism on human rights issues as well.

framing citizens through any means as outlawed; citizens have the right to demand compensation, according to law, for losses due to violation of their rights by any state organ or functionary

See Chapter Two of the 1982 Constitution, *translated in* 1 LAWS OF THE PEOPLES' REPUBLIC OF CHINA 1979-82 1 (1987).

²³³ Nevertheless, the discussions leading to their drafting and adoption showed a greater understanding of civil and political rights in China than was thought to have existed. The democracy movement was quashed not because civil and political liberties were deemed to be irrelevant to China's problems, but because the ruling party felt threatened by the persistent attacks on the political system that these rights seemed to engender.

Cohen, *supra* note 230, at 518-19.

²³⁴ *Id.* at 536-40.

²³⁵ This often has meant those countries receiving military or economic aid from the United States. See *International Protection of Human Rights: The Work of International Organizations and the Role of U.S. Foreign Policy: Hearings Before the Subcommittee on International Organizations and Movements of the House Committee on Foreign Affairs*, 93rd Cong., 1st Sess. (1973); *Human Rights in the World Community: A Call for U.S. Leadership: Report of the Subcommittee on International Organizations and Movement of the House Committee on Foreign Affairs*, 93rd Cong., 2nd Sess. (1974); *Human Rights and United States Foreign Assistance: Experiences and Issues in Policy Implementation (1977-1978): Report Prepared by the Foreign Affairs and National Defense Division, Congressional Research Service of the Senate Committee on Foreign Relations*, 96th Cong., 1st Sess. 52-53, 105-10 (1979).

²³⁶ See Cohen, *supra* note 230, at 528-36.

VIII. LOOKING TO THE FUTURE: HUMAN RIGHTS ADVANCEMENT
THROUGH GREATER INTEGRATION INTO THE WORLD
ECONOMIC COMMUNITY

The question of human rights is inextricably intertwined with the question of East-West economic relations.²³⁷ The Universal Declaration of Human Rights sets forth certain fundamental guarantees that should be provided for all persons, regardless of politics, race or nationality.²³⁸ Democracy, at its very minimum, recognizes these fundamental rights of man. Because these rights have been considered so important to the West, particularly the United States, the advancement of human rights should be an integral part of United States foreign policy. However, neither the President, the Congress, nor any other governmental institution of the United States can afford to act as a single purpose interest group to advance only human rights interests. The government must also take into account strategic, military, economic and other legitimate interests of the nation and mankind.

In dealing with communist nations or other nations that have had totalitarian control over their peoples, a goal of the United States generally has been to encourage political and human rights reform. Almost invariably, however, a nation's progress in political and human rights reform is linked to progress in the economic sphere. One does not necessarily precede the other; more commonly, they will develop in tandem. However, it is difficult for a developing country to focus upon democracy when the essential preoccupation is with the most basic requirements of food, clothing, housing or security.²³⁹

China, for example, tends to focus more on the economic and societal needs of the group in addressing human rights issues.²⁴⁰ In its efforts to encourage political and economic reform in a communist country with

²³⁷ The Reagan administration frequently highlighted the Soviet record on human rights. Testimony before Congress by two administration officials on July 14, 1987 indicated that no relaxation of the Jackson-Vanik amendment barriers to greater U.S. Soviet trade would be considered until the Soviets take concrete, positive steps towards emigration reform. *Jackson-Vanik Restrictions on MFN Benefits Not Likely to be Relaxed, Administration Says*, 4 Int'l Trade Rep. (BNA) 903 (July 15, 1987). During the May-June 1988 U.S. Soviet Summit meeting, President Reagan made a major point of raising the human rights issue.

²³⁸ *Universal Declaration of Human Rights*, G.A. Res. 217A, 3(1) U.N. GAOR Resolutions 71, U.N. Doc. A/810 (1948), reprinted in *HUMAN RIGHTS SOURCEBOOK* (A. Blaustein, R. Clark & J. Sigler eds. 1987).

²³⁹ China continues to struggle with the basic problems of poverty. *Deng Says China Must Concentrate on Ending Poverty*, China Daily, Oct. 14, 1987, at 1, col. 1.

²⁴⁰ See R. EDWARDS, L. HENKIN & A. NATHAN, *supra* note 225; *Notes on the Human Rights Question*, 22 BEIJING REV. 17-20 (Nov. 9, 1979); Baoxing, Chengquan, & Zervi, *On the Question of Human Rights in the International Realm*, 25 BEIJING REV. 13 (July 26, 1982).

a totalitarian tradition, the free world cannot expect success through mere exhortation, criticisms, and verbal attacks. Likewise, economic blockades and isolationism seldom have coercive effects on a strong nation. Such tactics tend to keep the target nation and its leadership on the defensive. It may in fact seal its defenses, as China sealed its doors to much of the Western world in the 1950s and 1960s and became an increasingly anti-United States, anti-Western, leftist nation.²⁴¹ First China, and more recently the Soviet Union, have expressed their desire to open their doors to the West, principally for economic reasons, but also for reasons of national security. Those nations are seeking an economic stake in the free world, although they have not yet expressed a willingness to join the free world fully with respect to political and human rights issues. This harbinger of the end of isolationism could serve the best interest of the globe both by reducing military and strategic tensions, and by improving world commerce. To give the communist nations an economic stake in the free world will, in effect, raise their future price of social deviance in the international community. Additionally, it will provide greater exposure to international norms of conduct which in turn will favorably influence reform efforts. Moreover, as economic conditions are raised in those countries, the expectations of the people will be raised, including democratic expectations.

A major obstacle to any rapprochement with either the Soviet Union or China has been the United States policy focus on human rights in those countries. The concern for human rights is so deeply embedded in the national psyche that it clearly cannot be abandoned. Moreover, the United States continues to enjoy a special place in the world of nations precisely because it is concerned about the rights of man. With increasing economic ties to Communist countries, the United States can insist upon compliance with international human rights norms, but that insistence must be realistically measured and credible. Inconsistency in United States policy, coupled with offensive, unfounded claims of human rights violations, will only be counterproductive. Similarly, United States policy makers must also take into account demonstrated sincerity in reform efforts.²⁴²

²⁴¹ In early 1988, Romania renounced its renewal of most favored nation status under the Jackson-Vanik Amendment to the 1974 U.S. Trade Act. Although the loss of MFN will likely cost Romania \$250 million dollars a year in lost exports, the Romanian move was in apparent protest to the emigration requirements of the Jackson-Vanik Amendment. *Romania Renounces Renewal of MFN Status, Move Follows Concerns Over Human Rights*, 5 Int'l Trade Rep. (BNA) at 286 (Mar. 2, 1988).

²⁴² According to the United States State Department's 1987 report on human rights around the world, the Soviet government gave its people greater freedom and showed more tolerance toward

In the realm of human rights, the more effective policy towards communist nations is their further integration into the world community, which in turn will raise the stakes of social deviance occasioned by domestic human rights violations. To insure that progress will be made on the human rights front, such integration should be gradual and measured, leaving no doubt that the human rights dimension is an important consideration in the normalization of economic relations.

IX. THE GEOPOLITICAL DIMENSIONS AND SOME CONCLUSIONS ABOUT THE PROSPECTS FOR A NEW STRATEGIC ECONOMIC POLICY TOWARDS THE EAST

One of the initial premises of this Perspective was that economic foreign policy and strategic foreign policy are inseparable, and therefore must be coordinated. A lingering and worrisome question that is yet to be answered is whether a stronger Soviet Union, built upon successful economic and political reforms, would increase the Soviet military threat against the United States and the rest of the free world. A related question is the effect on existing United States alliances if the Soviet Union is successful in its reforms. It has been suggested, for example, that the United States-Western Europe alliance remains strong because of the Soviet threat.²⁴³

Some commentators argue that any means of economic cooperation with the communist world must be assiduously avoided, and that we should take advantage of any weaknesses to frustrate Soviet economic reforms. One flaw in that argument is, of course, that the United States is not now in a position to totally frustrate those reforms, if it ever was. Such reforms have not occurred in the past, and the Soviet Union has remained relatively weak, not because of blockades or sanctions by the United States, but because of misguided Soviet policies and weakness of leadership. A major concern today is that while more effective leadership is in power, the underlying intentions of the ruling elite may remain unchanged.

dissenters during 1987, although there has been no "dawn of democracy." *U.S. Credits Soviets with Qualified Human Rights Progress*, St. Petersburg Times, Feb. 11, 1988, at 20A, col. 1.

²⁴³ If Gorbachev reduces the size of his army and convinces the allies that the Soviet Union poses no serious military threat, the problem of alliance cohesion will become more severe. Indeed, the problem goes much deeper. The inevitable economic conflict and tension *within* the western world has been easier to handle because of the sense of community created by the Soviet threat. A reduction in the perception of this threat will tend to bring the intrawestern economic conflicts more to the political fore. One can argue that this is probably already occurring, and that a major battle within the alliance on economic policy toward the Soviet Union will accelerate the process.

J. HOUGH, *supra* note 53, at 93.

The introductory portion of this Perspective addressed briefly certain notions about the Soviet Union that are deeply ingrained in United States foreign policy. Those perceptions will be difficult to change, particularly if the Soviet rhetoric on reform is not matched by tangible actions to reduce its pattern of hegemonistic ambitions. A corollary problem is that the Soviet leadership appears to have a deeply ingrained hostility towards the West generally, and the United States in particular, to this day.²⁴⁴

Because of this history of mutual hostility, any foreign aggression by the Soviets is interpreted as another step in the continuing aggression against the United States. The global reach of Soviet aggression has not made rapprochement easy in the past,²⁴⁵ and its contemporary extensions of power continue to pose barriers to any heightened economic cooperation in the future. The withdrawal of Soviet troops from Afghanistan removed a major obstacle to normalization of relations with the West, but the drama of that event alone fails to mask other substantial Soviet aggressions. The Soviet backed repression in Poland; Soviet involvement in promoting instability in Angola, Mozambique, Ethiopia, and other African nations, either directly, or through Cuba and other surrogates; its aid to the Sandinistas and other anti-United States groups in Central and Latin America; its relationship with bellicose Cuba, a mere ninety miles off Florida's coast; its involvement in Vietnam (which in turn is enabled to sustain its aggression in Cambodia); and other strategic incursions against United States interests and human rights abroad will insure the continuation of tensions.²⁴⁶ These questions, and corollary questions raised by the Soviets concerning United States actions abroad, must be on a continuing agenda for United States-Soviet dia-

²⁴⁴ See, e.g., *The Policy Behind Glasnost*, Asian Wall St. J., Feb. 2, 1988, at 6, col. 4. The 1917 Russian Revolution was based upon a fear and loathing of western institutions; the Tsar himself was in many ways viewed as more Western than Eastern. Because of their self-imposed isolationism, coupled with the West's policy of "containment" of communism, the Soviet Union and most other communist countries have not had significant contact with the West. While China made the transition towards integration into the society of free markets far more smoothly than many would have predicted ten years ago, the Soviet Union's transition likely will not be easy. There is hope that, although Soviet hostility towards Western democracies may not quickly dissipate, the hostility at least should become less provocative in light of Gorbachev's attempts for an East West economic rapprochement.

²⁴⁵ See *Economic Relations with the Soviet Union, 1982: Hearings Before the Subcomm. on Int'l Economic Policy & the Senate Comm. on Foreign Relations*, 97th Cong., 2d Sess. 45 (1982). Early experience under detente demonstrated that unless the Soviet Union has its own high stakes at risk, promises of good will within the context of detente are insufficiently reliable indicators of sincerity. During earlier periods of detente, Soviet troops invaded Czechoslovakia, and Soviet defense spending increased.

²⁴⁶ See *Soviet Pipeline Sanctions: The European Perspective, 1982: Hearings Before the Joint Economic Comm.*, 97th Cong., 2d Sess. 9, 12 (1982)(statement of Andra Fontaine).

logue if a true economic rapprochement is to be achieved. But they should not block the initiation of dialogue on improved economic relations. Positive steps in one arena will likely have positive results in another, be it strategic or economic.

It is encouraging that the Soviet Union appears to have shifted its policy with respect to Third World countries. The Soviet Union has begun to distance itself from terrorist and other radical activity, and to focus more on economic development. On the seventieth anniversary of the Bolshevik Revolution, Gorbachev in November 1987 condemned the views of Trotsky which had encouraged the export of revolution.²⁴⁷

As improved economic exchanges are considered, the stability of the Soviet regime and its reform efforts should be at the forefront of Western concerns. Under Mao Zedong, who ruled China's millions for more than a quarter of a century, proclamations of reform too often were followed by abrupt policy reversals which brought harsh punishment for those gullible enough to believe that the promised reforms were sincere and lasting.²⁴⁸

In contrast, the post-Mao era generally has been qualitatively different in significant respects. With each passing year, confidence in the permanence of China's economic reforms is building. Clearly, Deng Xiaoping, who effectively has held the reigns of power in China since 1978, is a reformist who is determined to replace the old order with a more modern, progressive and pro-Western leadership.

One of the most frequent topics of speculation among China watchers in the West has been what will happen after Deng passes from the scene. However, if Deng is successful in his efforts to establish the rule of law in China, his departure may not shake the foundations of the regime as earlier predicted. Deng already has been so successful in consolidating his reformist support that his philosophy may now be perpetuated without him. Zhao Ziyang, former premier and now Party chairman, clearly is a disciple of Deng and is one of the most eager aspirants for modernization in China. Li Peng, installed as premier during the October 1987

²⁴⁷ J. HOUGH, *supra* note 53, at 65-66. Hough also observed:

In 1987, however, Gorbachev was saying that a foreign policy that concentrated on revolution in such countries as Angola, Ethiopia, and Nicaragua, and on communist parties elsewhere, was conceding the big, non revolutionary countries such as Argentina, Brazil, Egypt, India, Indonesia, and Mexico to the United States and giving up on the prerequisites for an attack on protectionism that Soviet economic development required.

Id.

²⁴⁸ For example, in 1957, Mao announced the "Hundred Flowers Campaign," inviting intellectuals and others to come forward with their criticisms of the regime. When the response proved to be more than the regime could bear, the policy was immediately reversed and those who did speak out were severely punished.

Thirteenth Party Congress in Beijing, also is a reformer of Deng's persuasion, although apparently more moderate on modernization than Zhao Ziyang. At the 13th Party Congress, Deng was successful in achieving at least part of his aims to remove from office some of the older, more orthodox conservatives and replace them with younger and more progressive leaders. In short, there is good cause to conclude that the present regime in China, and its move to modernization, will experience a continuing period of stability.

The picture in the Soviet Union is quite different. The old style, anti-Western Soviet leadership has perpetuated itself throughout most of the nation's history, at least up to the regime of Gorbachev, which began a scant five years ago. Although it would be a mistake to assume there is any element of pro-Western sentiment in the Gorbachev philosophy, he clearly has recognized that some rapprochement with the West is essential in order to achieve the benefits of trade, investment, infusion of technology, and relief from the pressures of military buildup which are required for modernization of the Soviet Union. As was the case with China, rapprochement with the West is the only logical alternative.

Whether logic will prevail thus continues to be an open question as the United States ponders the ramifications of *perestroika* and *glasnost* in the Soviet Union. The success of Gorbachev's economic initiatives on the domestic front will have a direct bearing on his longevity as the nation's leader. Many observers expect that Gorbachev's reform efforts, both political and economic, will fall upon difficult times.²⁴⁹ As more dissent is invited by increased openness, hardliners will in turn urge harsh action when dissent becomes too difficult to handle. This can prove to be a special problem in Gorbachev's relationship with Eastern Europe, where the promises of restructuring and openness should have considerable appeal, yet pose an inherent conflict with continued Soviet domination.²⁵⁰ The specter of growing nationalism among the non-Russian elements of the Soviet state may be Gorbachev's single greatest domestic challenge. Those ethnic groups stand to gain a great deal by relaxed central control, introduction of market forces, and new policies of *glasnost*. As talk of democratization increases, the expectation levels of ethnic groups and satellite states may be raised to such an extent that latent dissension will erupt on the surface in open hostility to continued Soviet domination. The satellite states already are restive, and further talk of democracy may lead to open confrontations with Soviet authority.

²⁴⁹ See, e.g., E. HEWETT, REFORMING THE SOVIET ECONOMY: EQUALITY VERSUS EFFICIENCY (1988).

²⁵⁰ See generally Terry, Gorbachev, "Glasnost", and Eastern Europe, 1988 FLETCHER F. 253.

Some observers have concluded that China is now caught in the grip of a "revolution of rising expectations," in which the current reform program will never be able to satisfy the insatiable appetite it has created in the populace. In a climate of rising expectations, each failure fuels growing discontent.²⁵¹ Contemporary events in both China and the Soviet Union bear out such a thesis: by the end of 1987, student protests again occurred on Beijing's campuses.²⁵² In early 1988, riots erupted in Armenia in protest against Soviet government decisions,²⁵³ and protests were held in Hungary²⁵⁴ and in East Germany²⁵⁵ calling for more freedom. In early October, 1988, the Estonian Communist Party gave its blessings to the Popular Front of Estonia, an independent force that is demanding a capitalist-style economy.²⁵⁶

However, the power of the favored elite is deeply entrenched in the Party, government, and bureaucracy of both the Soviet Union and China. True reform is no picnic. It will mean divestiture of benefits from many of the powerful elite, and that will require more than mere exhortation. Thus, while the modernization program in China appears to be steady on course, the Soviet ship of state is only now leaving the harbor in its quest for *perestroika*. In spite of many early set-backs, however, Gorbachev now appears to be more in control than ever. On October 1st, 1988, he consolidated his leadership by taking over the Presidency of the country, further enhancing his role as head of the Communist Party.²⁵⁷ Three veteran members of the Party Central Committee, including incumbent President Andrei A. Gromyko, were retired and other conservatives ousted. Yegor K. Ligachev, the second highest official in the Party who has challenged Gorbachev's reformist policies in recent months, was moved to a less influential post.²⁵⁸

History teaches that the United States government, business, financial and investment communities must of necessity approach the communist world with a certain degree of caution. The universal benefits of peace and reduced tensions, however, justify a continued engagement of the Chinese and a prompt engagement of the Soviets and other nations of the communist world in a continuing dialogue over economic relations.

²⁵¹ *Peking Fuels Expectations It Can't Meet*, Asian Wall St. J., Jan. 7, 1988, at 6, col. 3.

²⁵² *Discontent Brews on China's Campuses*, Asian Wall St. J., Dec. 23, 1987, at 1, col. 3.

²⁵³ See *supra* note 206.

²⁵⁴ *Hungarians Call for Democracy and Free Press*, St. Petersburg Times, Mar. 16, 1988, at 13A, col. 3; *10,000, Crying "Democracy", March in Budapest*, N.Y. Times, Mar. 16, 1988, at A5, col. 1.

²⁵⁵ *E. Germans march for more freedom*, St. Petersburg Times, Mar. 16, 1988, at 13A, col. 5.

²⁵⁶ *Estonians Present Many Demands to Moscow*, New York Times, Oct. 2, 1988, at 11, col. 1.

²⁵⁷ *Gorbachev Named Soviet President, KGB is Reshuffled*, New York Times, Oct. 2, 1988, at 1, col. 6.

²⁵⁸ *Id.*

The potential is there for an unprecedented degree of East-West rapprochement. It is clear that any attempt at an economic rapprochement between the capitalist world and the communist world is fraught with difficulties and risks. However, the prospects for world peace and improved human conditions worldwide suggest that the effort must be made to end the strategic and economic deadlock between the East and the West.