US Treasury Department Designates China as a "Currency Manipulator" Under 1988 Statute

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Authors: Scott S. Lincicome, Brian Picone

On August 5, 2019, the US Department of the Treasury ("Treasury") announced that Treasury Secretary Steven Mnuchin, "under the auspices of President Trump," has determined that China is a "currency manipulator" pursuant to Section 3004 of the Omnibus Trade and Competitiveness Act of 1988 ("the 1988 Act").

The designation is largely symbolic, as the only remedy authorized by Section 3004 is the initiation of bilateral negotiations between the United States and the designated country. However, the Trump administration's decision to apply the designation to China at this time – just one week after the announcement that the United States will impose an additional 10 percent tariff on US$300 billion in annual Chinese imports as of September 1 – represents yet another escalation of the US-China trade dispute that likely will hinder further negotiations between the two countries.

Statutory criteria for currency manipulation

Section 3004 of the 1988 Act provides that the Treasury Secretary "shall analyze on an annual basis the exchange rate policies of foreign countries…and consider whether countries manipulate the rate of exchange between their currency and the United States dollar for purposes of preventing effective balance of payments adjustments or gaining unfair competitive advantage in international trade." The statute does not provide specific criteria for determining whether a country is engaging in such manipulation. Where a country is found to engage in manipulation, Section 3004 requires the Treasury Secretary to initiate negotiations with that country "on an expedited basis…for the purpose of ensuring that such countries regularly and promptly adjust the rate of exchange between their currencies and the United States dollar to permit effective balance of payments adjustments and to eliminate the unfair advantage." However, the law does not authorize further remedial actions. The Treasury Department has not labeled any country a "currency manipulator" under Section 3004 since 1994, when it last applied that designation to China.

Separately (and not cited in this case), Section 701 of the Trade Facilitation and Trade Enforcement Act of 2015 (TFTEA) requires Treasury to initiate "enhanced bilateral engagement" with any major US trading partner that: (i) has a significant bilateral trade surplus with the United States; (ii) has a material current account surplus; and (iii) has engaged in "persistent one-sided intervention in the foreign exchange market." If, within one year after enhanced bilateral engagement begins, Treasury determines that the country has failed to adopt appropriate policies to correct the alleged undervaluation and surpluses, the President is required to take one or more of the following remedial actions: (i) prohibit the Overseas Private Investment Corporation (OPIC) from approving any new financing with respect to a project located in that country; (ii) prohibit the US federal government from procuring goods or services from that country (except where such action would be inconsistent with US obligations under international agreements); (iii) instruct the US Executive Director of the IMF to call for rigorous surveillance of the macroeconomic and exchange rate policies of that country (and, as appropriate, formal

consultations on findings of currency manipulation); and/or (iv) instruct the US Trade Representative to take into account the country's alleged failure to cooperate when assessing whether to enter into a bilateral or regional trade agreement with that country. The President may choose not to take any remedial action, however, if doing so would adversely impact the US economy or national security.

The Treasury Department submits semi-annual reports to Congress assessing the foreign exchange practices of major US trading partners under the criteria set forth in Section 3004 of the 1988 Act as well as Section 701 of the TFTEA. In its most recent semi-annual report published in May 2019, Treasury stated that it "continues to have significant concerns about China's currency practices, particularly in light of the misalignment and undervaluation of the RMB relative to the dollar[.]" However, Treasury determined in the report that China "does not meet the standards identified in Section 3004 of the 1988 Act at this time" and "does not trigger all three criteria under [Section 701 of the TFTEA][.]"

August 5 determination under Section 3004

In its August 5 statement, Treasury cites the statutory standard for currency manipulation under Section 3004 of the 1988 Act, and states that "[i]n recent days, China has taken concrete steps to devalue its currency, while maintaining substantial foreign exchange reserves despite active use of such tools in the past. The context of these actions and the implausibility of China's market stability rationale confirm that the purpose of China's currency devaluation is to gain an unfair competitive advantage in international trade." The statement does not allege that China's foreign exchange practices satisfy the three criteria set forth in Section 701 of the TFTEA (which, as noted above, can trigger remedial actions), and does not otherwise reference Section 701. The statement therefore indicates that Treasury has found China to be a currency manipulator within the meaning of Section 3004 of the 1988 Act, and not under Section 701 the TFTEA. Treasury states that, as a result of its determination, Secretary Mnuchin "will engage with the International Monetary Fund to eliminate the unfair competitive advantage created by China's latest actions."

The designation does not appear to have any direct implications for the administration of the United States' trade remedy laws, including the countervailing duty statute, despite a recent US Department of Commerce ("Commerce") proposal that seeks to treat currency undervaluation as a countervailable subsidy. On May 23, 2019, Commerce published a proposed rule that, if adopted, would establish a process by which it may treat a foreign country's "currency undervaluation" as a countervailable subsidy for purposes of US countervailing duty proceedings, thus potentially subjecting imports from that country to remedial duties.[1] Treasury would play a central role in determining the extent of any currency undervaluation under the proposed rule. Nevertheless, the proposed rule targets currency "undervaluation" regardless of whether Treasury has made a statutory finding of "manipulation" with respect to the relevant country. It therefore is not clear that Treasury's determination will have any impact on countervailing duty proceedings in which the proposed rule is utilized, should it ultimately be adopted.

Outlook

Treasury's determination under Section 3004 does not trigger retaliatory trade actions by the United States, but it is one that China has aggressively resisted and is therefore likely to escalate bilateral tensions even further. Indeed, China has long sought to combat the perception that it has engaged in competitive devaluation of its currency, and it has cited the United States' own actions as the cause of the recent depreciation of the renminbi. (The People's Bank of China on August 5 cited "the effects of unilateralist and trade-protectionist measures and the expectations for tariffs against China" as the cause of the decline.) Independent observers like the International Monetary Fund, moreover, have recently found China's currency and current account to be broadly in line with market fundamentals. Coming just one week after the United States' announcement of new tariffs on

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[1] The proposed rule would newly "clarify" that (1) DOC "normally" will consider a benefit to be conferred upon a foreign producer or exporter when the domestic currency of the exporting country is undervalued in relation to the US dollar; and (2) all companies operating "in the traded goods sector of an economy" can constitute a group of enterprises for purposes of determining whether a subsidy is "specific" (and thus countervailable) under US law. See *Modification of Regulations Regarding Benefit and Specificity in Countervailing Duty Proceedings*, 84 FR 24406 (May 28, 2019).

US$300 billion in annual Chinese imports, the recent depreciation of the renminbi and the United States' reaction thereto signal further deterioration in the bilateral relationship and an expansion of the ongoing trade dispute to involve monetary policy. Such events could not only compound the dispute's economic impact but also worsen the prospects for its resolution.

The Treasury statement can be viewed here.

White & Case LLP
701 Thirteenth Street, NW
Washington, District of Columbia 20005-3807
United States

T +1 202 636 3600

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