

**TESTIMONY OF
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COMMITTEE ON ENERGY AND COMMERCE
SUBCOMMITTEE ON COMMERCE, TRADE AND CONSUMER PROTECTION
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Overview

Chairman Stearns, Congresswoman Schakowsky, Members of the Committee, I appreciate the opportunity to testify before the subcommittee today on the U.S.-China trade relationship. This is a subject of considerable importance to the Administration and the Office of the United States Trade Representative (USTR), in particular, in our capacity as the lead agency with responsibility for trade policy.

On December 11, 2001, after 15 years of negotiations with the United States and other World Trade Organization (WTO) members, China became a member of the WTO. Under the terms of its entry, China committed to implement a set of sweeping reforms designed to implement the WTO's market-oriented rules. It agreed to take concrete steps to remove trade barriers and open its markets to foreign companies and their exports in virtually every product sector and for a wide range of services. It also agreed to observe the WTO's national treatment standards, to protect and enforce intellectual property rights (IPR), to accept disciplines on the use of trade distorting subsidies and to make other changes to bring its legal and regulatory system in line with those of other WTO members and to add transparency and predictability to business dealings. China viewed joining the WTO as a means to preserve and expand China's access to export markets abroad, particularly the United States. In turn, other WTO members envisioned that faithful WTO implementation by China would reduce the ability of non-market forces, including government policies and officials, to intervene in the market to direct or restrain trade flows.

Total U.S.-China trade in 2003 topped \$180 billion, with imports from China exceeding U.S. exports by \$124 billion. China has now surpassed Japan and become the United States' third largest trading partner. China has become our second largest source of imports, with most of the increase displacing imports from other sources, including economies in Asia and Latin America. China has also become the sixth largest market for U.S. exports. In fact, China is currently the fastest growing export market for U.S. goods. Indeed, over the last three years, while U.S. exports to the world have decreased by 9 percent, exports to China have increased by 76 percent. China is now a major importer of U.S. manufactured exports, such as electrical machinery and numerous types of components and equipment, among other goods. China is also a major importer of agricultural products from the United States, and U.S. service suppliers in many sectors have been able to increase their share of China's market.

But, statistics are not the yardsticks by which the Administration measures China's compliance with its trade agreements. China's accession to the WTO, in particular, was conditioned on China's commitment to open its markets and to play by the rules of international trade. In that sense, the true measure of China's compliance with its WTO commitments is the extent to which China has institutionalized market mechanisms and curtailed direct governmental actions or complicity with non-governmental actions to intervene in the marketplace. By that score, China's WTO compliance record falls short of the mark.

As suggested in USTR's second annual Report to Congress on China's WTO Compliance, issued last December, China has made important headway since its WTO accession two years ago, and has completed much of the nuts and bolts work of WTO implementation. It has reviewed thousands of laws and regulations and made changes necessary to effect its new WTO obligations, established new transparency procedures in many national and sub-national ministries and agencies and the courts, and reduced tariffs to their committed levels, among other things.

Despite these gains, China's compliance with its WTO commitments has, over the past two years, been uneven at best. The Administration has engaged the Chinese government at every opportunity, whether through discussions in Washington or Beijing or at the WTO in Geneva, to address perceived shortcomings in Chinese WTO compliance. In some cases, USTR and other agencies were able to resolve U.S. concerns. For example, over the course of the past year, China has taken steps to correct systemic problems in its administration of the tariff rate quota system for bulk agricultural commodities. It relaxed certain market constraints in soybeans trade that allowed U.S. exporters to achieve record sales. It reduced capitalization requirements in certain financial services sectors. It opened up the motor vehicle financing sector. It solved outstanding concerns that had prevented China's membership in the WTO's Committee of Participants in the Expansion of Trade in Information Technology Products.

In its first year of WTO membership, China's incomplete implementation of WTO commitments could in some cases be attributed to start-up problems or incomplete understanding of WTO rules and practices. These rationales are less meaningful two years into WTO membership, however. In fact, while China made significant initial strides toward WTO implementation in its first year, China's WTO efforts seemed to have lost a significant amount of momentum last year. Indeed, in a number of different sectors, including some key sectors of economic importance to the United States, some Chinese ministries seemed to spend as much energy avoiding China's WTO obligations as living up to them. Institutionalized market mechanisms remain elusive, and intervention by Chinese government officials in the market is largely unchecked.

We acknowledge that China's WTO implementation efforts have taken place against a challenging political and social backdrop. In 2003, China underwent a major leadership change, passed through a harrowing national SARS epidemic, undertook a sizeable restructuring of the government's economic and trade functions, and confronted a host of dislocations inherent in its transition from a planned economy to a more market oriented economy. These factors may have

presented challenges, but they are not grounds for foot dragging or other incomplete WTO implementation efforts.

Our markets are certainly open to exports from Chinese companies, and we need to ensure that China operates with fair, transparent and predictable rules when it comes to our companies' access to China's market. That means, most importantly, that China must live up to the commitments that it made upon joining the WTO. We also need to ensure that China engages in fair trade when it comes to its exports to the United States. Our companies want, and are entitled to, a level playing field.

U.S. Management of WTO Implementation Concerns

The Administration has stepped up its efforts to engage senior Chinese leaders. Over the course of the past year, as China's WTO implementation progress has slowed, President Bush met with the current President of China, Hu Jintao, and emphasized the importance of China's WTO obligations. United States Trade Representative Zoellick made two separate visits to China for talks on WTO implementation matters with China's Premier, Wen Jiabao, and Vice Premier Wu Yi. The Secretaries of Commerce and Treasury made similar trips to China, again carrying the message that China's WTO implementation was a matter of the highest priority. Sub-cabinet officials from various U.S. economic and trade agencies also met with their Chinese counterparts in China, Washington and Geneva to work through areas of concern, including WTO implementation issues, on numerous other occasions.

In 2003, the Administration also utilized the newly established sub cabinet dialogue on WTO compliance and other trade matters (the Trade Dialogue), which brings together U.S. economic and trade agencies and various Chinese ministries and agencies with a role in China's WTO implementation. Trade Dialogue meetings were convened twice in 2003, once in February, led by then Deputy United States Trade Representative Huntsman, and later in November, led by Deputy United States Trade Representative Josette Sheeran Shiner. The Trade Dialogue meetings have proven to be effective venues for raising, and seeking the resolution of, specific trade concerns, and in serving as an early warning mechanism for emerging trade disputes.

This year, in a concerted effort to solve bilateral trade issues, the United States and China agreed to elevate the annual Joint Commission on Commerce and Trade (JCCT) talks, with United States Trade Representative Zoellick and Commerce Secretary Evans chairing the U.S. side and Vice Premier Wu Yi chairing the Chinese side. Over the past three months, through a series of meetings in Beijing and Washington leading up to the April 21 talks, staff from USTR and the Commerce Department have been working with their Chinese counterparts to achieve tangible progress on the key issues. We are pressing China to take major, concrete steps in a number of areas where China's WTO compliance has been lagging, including:

- \$ Substantially improved enforcement of intellectual property rights in China, including through the use of deterrent-level criminal penalties, and the crackdown on those who export or traffic in counterfeit or other IPR-infringing products;
- \$ China's full adherence to commitments to open its agricultural market and to refrain from the use of arbitrary limitations on market access, including sanitary and phytosanitary measures and other restrictions not based on science;
- \$ The removal or modification of discriminatory aspects of Chinese industrial policies and other measures that fail to accord U.S. and other WTO member firms national treatment and fair market access, particularly with regard to integrated circuits and wireless encryption technology;
- \$ The lifting of excessive restrictions imposed by China's regulators on foreign service suppliers;
- \$ China's use of fair and transparent technical standards and regulations, including the establishment of procedures that guarantee the public's right to notice and comment; and
- \$ Full and timely liberalization in the areas of trading rights and distribution services.

Of course, while we prefer to resolve our concerns through collaborative mechanisms like the JCCT, we are not hesitant to use other means when necessary. Indeed, there are forces in China, as elsewhere, that are resistant to the changes wrought by WTO implementation. Despite the best of intentions of many Chinese trade officials, these forces have not been unsuccessful in limiting China's progress toward the goals the United States and other WTO members foresaw through China's WTO accession. As a result, some markets in China are not as open as they should be, and our engagement with China has not always been as useful as it should be.

One area where collaboration has not been successful affects key U.S. technology products, namely, integrated circuits. China provides preferential value-added tax treatment to integrated circuits produced or designed in China, thereby disadvantaging U.S. and other imports and distorting international investment. The United States believes that this discriminatory tax policy is inconsistent with the national treatment obligations that China assumed when it joined the WTO. The United States has repeatedly pressed its concerns with China, but it recently became clear that China was not prepared to address our concerns in any meaningful way. As a result, on March 18, 2004, the United States filed a case at the WTO regarding China's policy. This move commences a 60-day consultation period required by WTO rules. If a resolution cannot be reached within that time period, we can then request that a WTO panel rule on whether China's policy is consistent with its WTO obligations.

Enforcement of Trade Remedies Laws

The rapid expansion of trade between our two countries has inevitably led in some cases to competition between our domestically produced goods and Chinese imports. When our industries face injurious trade with China, the Administration is fully committed to enforcing U.S. trade remedy laws and to exercising the important rights that the United States has under China's WTO accession agreement.

One of our tools is the use of the antidumping laws, which, under the terms of China's WTO accession, includes our ability to continue to apply a special non-market economy methodology to China. In 2003, more than 50 percent of antidumping orders put in place by the Department of Commerce involved Chinese imports.

China also agreed to two separate China-specific safeguard mechanisms as part of its WTO accession package. These mechanisms are designed to allow WTO members to cope with market disruptions caused by increasing economic integration with China following its WTO accession.

One of the safeguards agreed to by China is specific to textiles. It allows WTO members under certain circumstances to invoke limited import relief against Chinese imports. Specifically, a 7.5 percent cap on growth in imports of a given textile category for up to one year (6 percent for wool products) until December 31, 2008. Late last year, the Committee for Implementation of Textile Agreements found for the petitioners in all three of the investigations that it conducted and, in December, the import relief contemplated by the safeguard went into force.

Another safeguard, now codified in U.S. law as Section 421 of the Trade Act of 1974, as amended, applies to any product imported from China and is available until December 11, 2013. Since the implementation of Section 421, five petitions have been filed requesting the imposition of import restrictions. In two cases, the U.S. International Trade Commission (ITC) found that our domestic producers' market had not been disrupted by imports from China. In three other cases, while the ITC found market disruption, the President weighed the costs and the benefits to the U.S. economy, as the statute contemplates, and determined that the adverse impact on the U.S. economy was clearly greater than the benefits of import restrictions. While to date no import relief has been granted under Section 421, the President, in his most recent determinations, has reiterated his commitment to using this safeguard when the circumstances of a particular case warrant.

Conclusion

While the U.S.-China economic and trade relationship is growing rapidly, there are a number of structural impediments that remain, making further improvements in that relationship problematic. The Administration is committed to resolving the United States' concerns through all available means. It will use bilateral engagement, whenever possible. For the most part,

bilateral efforts have been effective or continue to hold some near-term likelihood of success. However, when those efforts are not productive, or it becomes clear that bilateral engagement on a particular issue has reached stasis, as in the case of China's tax policy on integrated circuits, the Administration is fully prepared to assert the United States' rights under U.S. law and through multilateral means, including dispute settlement at the WTO.