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I. INTRODUCTION

In the ten years since it acceded to the World Trade Organization ("WTO"), China has engaged in a consistent pattern of avoiding, delaying, and directly violating its WTO commitments. China's systematic failure to comply with its WTO obligations has adversely impacted the U.S. and global economies and undermines the legitimacy of the international rules-based trading system.

When China formally acceded to the WTO on December 11, 2001, it agreed to be bound by provisions of the existing WTO agreements, in addition to commitments specific to China negotiated in its Protocol of Accession to the WTO ("Accession Protocol"), the accompanying Report of the Working Party on the Accession of China ("Working Party Report"), and the schedule of China's commitments on market access for goods and services. These agreements contain binding obligations on the provision of government subsidies, treatment of state-owned enterprises ("SOEs"), various import and export restrictions, non-discrimination against foreign entities, and many other issues. While China has made some progress toward achieving some of its WTO commitments, many of its obligations remain unfulfilled and, in a number of respects, the Chinese government is moving further away from compliance. In fact, China is increasingly manipulating the WTO system, exploiting loopholes and working around existing rules – in violation of the spirit, if not the letter, of the WTO agreements.

Leading up to China's 2001 accession, many in the United States and around the world believed China's WTO membership would bring it into compliance with an enforceable, rules-based international trading regime, providing substantial benefits for all WTO Member countries. Many expected that China's WTO entry would lead to the opening of Chinese markets to foreign products and investment, by reducing Chinese tariffs and addressing non-tariff trade and investment barriers. In the United States in particular, proponents of Chinese

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WTO membership claimed that it would create U.S. jobs, increase U.S. exports and improve the trade deficit with China. For example, President Clinton claimed in 2000 that China's WTO accession agreement "creates a win-win for both countries."

Unfortunately, because China has substantially failed to comply with many of the commitments it made upon acceding to the WTO, most of these anticipated benefits for the United States have not been realized. China's ongoing trade-distorting practices, including massive subsidies, growing state ownership and control over key segments of the economy, export restrictions on raw materials, and manipulation of its currency, have prevented the flow of U.S. exports to China and the increase in U.S. jobs expected upon China's WTO accession. Moreover, the fact that the world's second largest economy continues to flout many of its WTO commitments and other trade norms serves to undermine the legitimacy of the international rules-based trading system.

II. SINCE ITS ACCESSION, CHINA HAS SYSTEMATICALLY VIOLATED ITS WTO COMMITMENTS

A. The Chinese Government Provides Significant WTO-Inconsistent Subsidies to Its Domestic Industries

Upon its accession to the WTO, China assumed the obligations of the WTO Agreement on Subsidies and Countervailing Measures ("SCM Agreement").[2] In particular, China committed that, by the time of its accession, it would eliminate all subsidies prohibited under Article 3 of the SCM Agreement – specifically, those contingent on export performance and on the use of domestic over imported goods.[3] In addition to export and "local content" subsidies, China agreed not to cause, through the use of any subsidy, (i) injury to the domestic industry of another Member, (ii) the nullification and impairment of benefits accruing directly or indirectly to another Member, or (iii) serious prejudice to the interests of another Member.[4]

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2 WTO Working Party on the Accession of China, *Report of the Working Party on the Accession of China*, WT/ACC/CHN/49 ¶¶ 166-68, 171,174 (Oct. 1, 2001), *available at* http://unpan.org (last visited Sept. 7, 2011) ("Working Party Report"); *see also* World Trade Organization, *Accession of the People's Republic of China: Decision of 10 November, 2001*, WT/L/432 ¶¶ 10.3 (Nov. 23, 2001) ("China Protocol of Accession").

3 Working Party Report ¶¶ 166-68, 171, 174; China Protocol of Accession ¶ 10.3. *See also* Agreement on Subsidies and Countervailing Measures, Apr. 15, 1994 at Art. 3.1(a)-(b) ("SCM Agreement"), Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, Legal Instruments—Results of the Uruguay Round, 33 I.L.M. 1125 (1994).

4 SCM Agreement at Art. 5.

Despite these specific commitments, China continues to grant massive subsidies to its domestic industries in violation of its WTO obligations.[5] Over the past year, the Department of Commerce has found in various countervailing duty cases that the Chinese government subsidizes many of its domestic industries, including through the provision of inputs for less than adequate remuneration, direct transfers of government funds, preferential lending through state-owned commercial or policy banks, and preferential tax treatment.[6]

The bulk of the subsidies are granted to SOEs in pillar industries, with the aim of creating large, internationally competitive "national champions." For example, the Chinese government continues to grant massive subsidies to Chinese steel companies, pursuant to government directives and in violation of its WTO commitments. A 2007 report identifies more than $52 billion in subsidies granted to Chinese steel producers.[7] These documented subsidies include $17.3 billion in preferential loans and directed credit, $18.6 billion in equity infusions and/or debt-to-equity swaps, $5.1 billion in land-use discounts, $1.3 billion in government-mandated mergers, and $258.6 million in direct cash grants.[8] These massive government subsidies have helped to create the world's largest steel industry and explain why China's steel exports (particularly exports to the United States) have increased significantly during the past decade. With its total steel production now more than eight times larger than that of the U.S. steel industry, China's exports to the United States and the rest of the world will only increase.[9]

China's most recent national industrial plan, the 12th Five-Year Plan ("FYP"), provides for the continuation of massive subsidies to key industries. The plan, covering the period 2011-2015, mandates subsidies ranging from preferential tax and financing policies to the establishment of "funds" for certain industries.[10] Beneficiaries include small to medium size

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5 *2010 Report to Congress on China's WTO Compliance* at 11, United States Trade Representative Office, Dec. 2010. USTR's 2010 Report to Congress on China's WTO Compliance confirms that "China continues to provide injurious subsidies to its domestic industries."

6 *See, e.g.*, *Drill Pipe from China*, 76 Fed. Reg. 1,971 (Dep't Commerce Jan. 11, 2011) (final affirmative countervailing duty deter, final affirmative critical circumstances deter.).

7 *Money for Metals: A Detailed Examination of Chinese Government Subsidies to its Steel Industry,* Wiley Rein LLP, Jul. 2007, *available at* http://www.wileyrein.com/public_document.cfm?id=16051 at iii and 3.

8 *Id*. at iii-iv.

9 *See The Reform Myth: How China is Using State Power to Create the World's Dominant Steel Industry*, Wiley Rein LLP, Oct. 2010 ("Reform Myth"), *available at* http://www.wileyrein.com/resources/documents/Reform_Myth.pdf at 2-3.

10 China's Twelfth Year Plan (2011-2015) at Chapter 1.

enterprises ("SMEs"), China's seven strategic and emerging industries (such as clean energy), and the manufacturing sector. The 12th FYP is further demonstration that the Chinese government does not intend to bring its behavior into compliance with its WTO commitments with respect to subsidies in the near future.[11]

B. <u>The Chinese Government Continues to Heavily Intervene in the Commercial Decisions of Its State-Owned Enterprises, Contrary to Its WTO Commitments</u>

During the course of its accession to the WTO, the Government of China committed that it "would not influence, directly or indirectly, commercial decisions on the part of state-owned or state-invested enterprises."[12] China further agreed to ensure that all state-owned and state-invested enterprises would make purchases and sales "based solely on commercial considerations"[13] and to run its SOEs, including banks, on a commercial basis, making these SOEs "responsible for their own profits and losses."[14] Given the pervasiveness of state ownership in China, these were some of China's most important commitments upon accession.

Despite these clear commitments, the Chinese government continues to exercise considerable government ownership and control over key segments of its economy and continues to heavily intervene in the commercial decisions of its SOEs for the purpose of advancing government aims. As U.S. Ambassador to China Gary Locke recently stated, "China seems to be embracing state capitalism more strongly each year rather than continuing to pursue economic reform goals."[15]

In fact, since its accession to the WTO, the Chinese government has taken a number of legal and administrative measures to increase its ownership and control over its SOEs, in blatant

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11 China has also violated its obligation to notify WTO Members of all subsidies it imposes. China did not submit its first subsidies notification until April 2006 – nearly five years after joining the WTO. That subsidies notification, which USTR described as "notably incomplete," covered only the period from 2001 to 2004 and "failed to include any subsidies provided by local and provincial government authorities," which are substantial in China. *See* Joint Report of the Office of the United States Trade Representative and the U.S. Department of Commerce: *Subsidies Enforcement Annual Joint Report to Congress* (Feb. 2010). On October 21, 2011, more than five and a half years after its first notification, China finally submitted its second subsidies notification to the WTO. Again, the notification lists only central government subsidies and covers the limited time period of 2005 to 2008.

12 Working Party Report ¶ 46.

13 *Id.* ¶ 44.

14 *Id.* ¶ 172.

15 Sophie Leung, *U.S. Troubled By Growing China Intervention in Trade, Locke Says,* Bloomberg (Dec. 5, 2011).

violation of its WTO commitments. For example, in 2003, the Chinese government established the State-owned Assets Supervision and Administration Commission of the State Council ("SASAC") to exercise ownership rights over China's largest SOEs. SASAC enables the Chinese government to exercise considerable control over the commercial decisions of SOEs, including decisions relating to their strategies, management, and investments.[16] China's recently issued 12th FYP further demonstrates the government's continued and substantial involvement in the economy, providing for direct government ownership and control over certain sectors of the economy. The plan explicitly states that one of its goals is to "uphold the basic economic system in which public ownership is the mainstay."[17] Specifically, the plan provides for the following: enhanced government supervision, control, and direction over SOEs;[18] the development of large, internationally competitive national champions (the vast majority of which are SOEs);[19] and increased regulation of state-owned capital and SOEs' financial performance.[20]

The Chinese steel industry provides a particularly compelling example of China's substantial ownership and control over its SOEs. Government ownership and control of the steel industry has grown dramatically since China's accession to the WTO in 2001, and continues to increase, despite its commitments regarding market reforms. Specifically, in 2007, 91 percent of the production of the top 20 steel groups was state-owned and controlled.[21] By the end of 2009, more than 95 percent of the production of those steel groups was subject to some government ownership.[22]

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16 *See* 2010 USTR Report to Congress on China's WTO Compliance at 59.

17 Chapter 45 of Title XI in China's Twelfth Five-Year Plan (Reform in Different Areas, Improving Socialism Institution of Market Economy) ("China's 12th FYP").

18 China's 12th FYP seeks to "advance the strategic restructuring of the state-owned economy and improve the mechanisms for redirecting investments of state capital to ensure its rational flow." It also seeks to "advance state capital to focus on key fields which involve national security and national economic lifelines" and to "improve the management of state-owned assets and the SOE supervision system." Title XI, Chapter 45 and Title XI at 1 and 2.

19 China's 12th FYP states that the government will direct and encourage mergers and acquisitions, including by "promot[ing] integration between strong enterprises and trans-regional mergers and acquisitions among superior enterprises to enhance industrial concentration" and "rationally provid[ing] guidance to the merging and reorganization of enterprises." Chapter 9, Title III at sec. 4 and Chapter 4 at 12, October version.

20 Title VIII, Chapter 32 at 1 and 2. The FYP also states that "the investment behavior of state-owned enterprises should be standardized." Chapter II at 7.

21 *See Money for Metal: A Detailed Examination of Chinese Government Subsidies to the Steel Industry*, Wiley Rein, LLP, Jul. 2007 ("Money for Metal"), *available at* http://www.wileyrein.com/resources/documents/pu4411.pdf at 8-10.

22 *See* Reform Myth at 6.

The Chinese government also exercises extensive control over its steel-producing SOEs through policy instruments which afford the government substantial leverage to direct the evolution of the industry. In fact, since 2005, the government has issued a number of industrial plans and other policy directives specifically covering the steel industry that have significantly increased government control over the development of the industry, in direct violation of China's WTO commitments.[23] Most recently, China's 12th Five-Year Plan for the Iron and Steel Industry (the "Steel Plan"), issued October 24, 2011, allows the Chinese government to direct and control virtually every aspect of its largely state-owned industry, including resource and equipment utilization, output levels, product quality improvements, technological innovation, and consolidation within the industry. The Steel Plan is yet another example of China intervening heavily in the decision-making of its steel-producing SOEs in a manner inconsistent with its WTO obligations.

China's massive government ownership and control has allowed for the creation of the world's largest steel industry. In fact, China has captured all the world's growth in steel production over the last decade, with Chinese production increasing by almost 350 percent from 2000 to 2009,[24] while production in the rest of the world decreased by 10 percent.[25] This growth has had nothing to do with commercial considerations. In fact, China is critically deficient in many steel-making raw materials and labor is not a major cost factor in today's steel industry. The dramatic increase in China's steel production has occurred despite the fact that the Chinese steel industry has experienced financial returns that are the lowest of those achieved by any other major steel industry around the globe and well below Chinese industry as a whole. As a result, the growth of the Chinese steel industry cannot be explained by market forces. Rather, its tremendous growth has been a result of massive government support for and intervention in its steel-producing SOEs, contrary to its WTO obligations.[26]

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23 These plans include the 2005 Steel and Iron Industry Development Policy, the 2009 Steel Adjustment and Revitalization Plan, and the June 2010 State Council Policy, as well as central and provincial government five-year plans. For additional information with respect to these policies, *see* Reform Myth at 11-17.

24 *See* Reform Myth at 2, 4.

25 *Id*.

26 The George W. Bush Administration led significant efforts to eliminate government ownership from the global steel industry in order to reduce market distortions. With the exception of China, these efforts were largely successful. However, as a result of the unprecedented growth of Chinese government steel companies, the percentage of the global steel industry subject to government ownership is currently at its highest levels.

The steel industry is but one example of China's efforts to increase government ownership and control over its key industries so as to achieve governmental, rather than market, aims. The Chinese government, for example, is actively working to "consolidate" the rare earths industry into three primary enterprises so as to enhance its ownership and direction over the industry. Indeed, many of China's key industries have undergone forced consolidation, often in the name of environmental protection. In reality, however, the consolidation is designed to enhance the government's ownership and control over key industries.

C. China Imposes a Variety of Market-Distorting and WTO-Inconsistent Export Restrictions

The GATT 1994 generally prohibits WTO Members from maintaining export restrictions (other than duties, taxes or other charges).[27] As part of its WTO accession, China further agreed to eliminate all taxes and charges on exports other than those listed in Annex 6 to its Accession Protocol or those applied in conformity with Article VIII of the GATT 1994.[28] However, in clear violation of these commitments, China imposes export quotas, export taxes, export licensing regimes, and other measures to limit its exports, including exports of critical raw materials. China also imposes minimum export prices on certain raw materials.

In fact, in July 2011, a WTO dispute settlement panel ruled in a case brought by the United States that China's maintenance of export restrictions on various raw materials (such as bauxite, coke, and zinc) is inconsistent with its WTO obligations and recommended that China come into compliance with its commitments.[29] In particular, China's use of export duties was found to violate its agreement to eliminate all taxes and charges applied to exports, with a few narrowly-delineated exceptions.[30] The WTO panel specifically rejected China's arguments that it was allowed to justify its export taxes as measures necessary to protect human, animal or plant life or health[31] or as measures relating to the conservation of exhaustible natural resources.[32] China appealed the ruling, and an Appellate Body decision is expected in the coming months.

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27 GATT Art. XI; Working Party Report ¶¶ 166-68, 171, 174.

28 *Id.* *See also* GATT Art. VIII only permits fees and charges limited to the approximate cost of services rendered and makes clear that any such fees and charges shall not represent an indirect protection to domestic products or a taxation of exports for fiscal purposes. *Id.* This article is not relevant for the present discussion.

29 *See* Panel Report, *China – Measures Related to the Exportation of Various Raw Materials*, WT/DS394/R, WT/DS395/R, WT/DS398/R (July 5, 2011).

30 *See* China Protocol of Accession.

31 *See* GATT Art. XX(b).

Despite this ruling and its long-standing commitments, China continues to impose WTO-inconsistent export restrictions on a variety of raw materials, including on rare earth elements. These measures are designed to keep critical raw materials in China and to advantage Chinese producers at the expense of producers around the globe. These export restrictions are also used to entice rare earth-consuming industries to relocate to China. While the environment may be used as an excuse to defend its actions at the WTO, companies have little trouble getting rare earths at lower prices and in sufficient quantities if they relocate production to China. These types of market-distorting practices are contrary to WTO principles.

D. China's Manipulation of Its Currency Constitutes a Violation of Its WTO Commitments

China continues to control the exchange rate between its currency (the "renminbi" or the "yuan") and the U.S. dollar, encouraging a large trade surplus with the United States.[33] Specifically, the Chinese government maintains an exchange rate policy by which it pegs the value of the yuan to a basket of foreign currencies heavily weighed by the U.S. dollar. China's government intervention in the valuation of its currency makes the yuan artificially cheap relative to the dollar, lowering China's cost of production relative to the United States. In this way, the type of currency manipulation practiced by China unfairly benefits its domestic industries and actively promotes the export of Chinese manufactured products.[34]

China's currency undervaluation thus constitutes a countervailable subsidy under the WTO's SCM Agreement, as it constitutes a financial contribution by the Chinese government, which confers a benefit upon its recipient.[35] Moreover, consistent with the WTO ruling in *United States-Tax Treatment for "Foreign Sales Corporations,"* China's currency manipulation appears to be a prohibited export subsidy because it is designed to principally benefit China's exporters.[36] When Chinese producers export their product to the United States, they receive

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[32] *See* GATT Art. XX(g).

[33] *See* Robert E. Scott, *Growing U.S. Trade Deficit with China Cost 2.8 Million Jobs Between 2001 and 2010*, Economic Policy Institute, Briefing Paper #323 (Sept. 20, 2011) at 4.

[34] Congressional Record-Senate: Currency Exchange Rate Oversight Reform Act of 2011, 157 Cong. Rec. S6020 (Oct. 3, 2011).

[35] *See* SCM Agreement at Art. 1.1.

[36] *United States - Tax Treatment for "Foreign Sales Corporations" - Recourse to Article 21.5 of the DSU by the European Communities - AB-2001-8*, WT/DS108/AB/RW ¶ 119 (Jan. 14, 2002).

payment in U.S. dollars, which they are required to trade for Chinese yuan.[37] Given the Chinese government's manipulation of its exchange rate for purposes of maintaining an undervalued yuan, exporters receive more yuan per dollar than they would receive if China permitted its exchange rate to fluctuate freely. Most estimates place this subsidy at roughly 28.5 percent of the U.S. dollar, even after recent appreciation in the yuan,[38] although some estimates value the subsidy at as much as 50 percent.[39]

In addition to being an impermissible export subsidy, China's currency manipulation is also actionable at the WTO because it nullifies and impairs the benefits accruing to the United States under GATT 1994,[40] and because it frustrates the intent of the WTO agreements, under GATT Art. XV(4).[41] Economists and policymakers alike agree that China's currency policies have enabled it to amass an enormous trade surplus with the United States to the clear detriment of U.S. manufacturers.[42] As Senator Jeff Sessions recently testified:

> So our goods that go there are higher in China than they would be, making the Chinese less able to buy them than otherwise would be the case. The goods they ship to the United States come in cheaper than they otherwise would be, making them more attractive to American consumers. This is a big factor in the surging and huge trade deficit between our countries.[43]

Echoing these sentiments, Senator Harry Reid testified that China's currency undervaluation "hurts our economy and it costs American jobs. In the last decade alone, we have lost more than 1 million American jobs to China because of this trade deficit fueled by currency manipulation."[44]

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[37] *See* 2010 Report to Congress of the U.S.-China Economic and Security Review Commission, 111th Cong., 2d Sess. (Nov. 2010) at 3-4.

[38] Robert E. Scott, *Growing U.S. Trade Deficit with China Cost 2.8 Million Jobs Between 2001 and 2010*, Economic Policy Institute, Briefing Paper #323 (Sept. 20, 2011) at 5.

[39] *See* CRS Report for Congress, *China's Currency: An Analysis of the Economic Issues*, RS21625 (Aug. 3, 2011).

[40] *See* SCM Agreement at Art. 5; GATT Art. XXIII.

[41] *See* GATT Art. XV(4).

[42] *Id*.

[43] Congressional Record-Senate: Currency Exchange Rate Oversight Reform Act of 2011, 157 Cong. Rec. S6020 (Oct. 3, 2011).

[44] *Id.*

In fact, the Chinese government openly acknowledges that it undervalues its currency to create jobs and to help its export-based industries. For example, *China Daily*, the government-run newspaper, stated last month that "[i]f the yuan rises too fast, many migrant workers in export enterprises would lose their jobs, for their employers would go bankrupt because of a severe shortage of export orders. This would harm China's consumer market and pose a great challenge for its economy."[45] This demonstrates that China's currency policy is designed to unfairly advantage domestic Chinese industries in world trade to the detriment of economies around the globe, contrary to the WTO's rules-based and non-discriminatory system. As such, China's currency manipulation serves to nullify and impair the anticipated benefits to the U.S. and other global economies from China's WTO accession.[46]

E. The Chinese Government Engages in Various Other Trade-Related Practices Which Violate Its WTO Commitments

- Government Procurement Agreement ("GPA"): China has failed to take the steps necessary to accede to the GPA, although it committed to enter into negotiations to join as part of its WTO accession.[47] China recently submitted its second revised offer for acceding to the GPA negotiations, but the offer fails to cover major segments of the Chinese procurement process, such as coverage of SOEs and an expansion of services coverage.[48] China's membership in the GPA could open up the significant Chinese government procurement market to foreign companies and bring China's domestic procurement regulations into line with international rules.

- Indigenous innovation: Government policies intended to promote "indigenous innovation" are pervasive in China, to the disadvantage of foreign companies and in violation of China's WTO obligations. For example, in its Accession Protocol, China agreed to "eliminate and cease to enforce" mandatory technology transfer requirements made effective through laws, regulations or other measures.[49] However, in many instances, the Chinese government continues to require the transfer of technology as a condition of approval for foreign investment projects in China.[50]

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45 Deng Yuwen, *No Winners in a Trade War*, China Daily, Nov. 15, 2011.

46 *See* GATT Art. XXIII.

47 Working Party Report ¶ 349; China Protocol of Accession ¶ 1.2.

48 *See New Chinese GPA Offer Covers Some Sub-Central Entities, But Shows Few Other Concessions*, Inside U.S. Trade (Dec. 5, 2011).

49 China Protocol of Accession ¶ 7.3.

50 *See*, *e.g.*, Trade Laws Advisory Group, *China's Laws Regulations and Practices in the Areas of Technology Transfer, Trade-Related Investment Measures, Subsidies and Intellectual Property Protection Which Raise WTO Compliance Concerns* (Sept. 2007).

- Intellectual property rights: Upon China's accession to the WTO, it committed to provide effective protection of intellectual property rights and to abide by the WTO's Agreement on Trade-Related Aspects of Intellectual Property Rights ("TRIPS Agreement").[51] However, as USTR notes, "China has continued to demonstrate little success in actually enforcing its [intellectual property] laws and regulations in the face of the challenges created by widespread counterfeiting, piracy and other forms of infringement."[52]

- Circumvention of U.S. trade orders: There is widespread evidence that Chinese manufacturers whose products are subject to antidumping ("AD") or countervailing duty ("CVD") orders in the United States have attempted to illegally circumvent or evade the payment of duties owed. U.S. steel producers, as well as companies in other industries, have repeatedly brought evidence of China's trade law circumvention to the attention of U.S. Customs and Border Protection ("CBP").[53] Chinese companies circumvent AD and CVD orders through a variety of means, including illegal transshipment of goods through third countries, falsified country of origin markings, undervalued invoices that offset the payment of AD/CVD duties, and the misclassification of goods.[54]

- Transparency issues: Transparency is a core principle throughout the WTO agreements, and many of China's accession commitments involve increasing transparency in China's legal system and in the application of its laws. For example, China agreed to provide a reasonable period for public comment on many new or modified laws and regulations before implementing them.[55] However, despite some improvements in this area, "a significant number of departmental rules are still issued without first having been published for public comment on the State Council's website."[56] Also with regard to notifying the public of new laws and standards, China "still does not appear to notify all new or revised standards, technical regulations and conformity assessment procedures as required by WTO rules."[57]

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51 China Protocol of Accession at Annex 1A.

52 USTR 2010 Report to Congress on China's WTO Compliance (Dec. 2010) at 83.

53 *See*, *e.g.*, Statement of Karl G. Glassman, Chief Operating Officer of Leggett & Platt, Before the U.S. Senate Subcommittee on International Trade, Customs, and Global Competitiveness (May 5, 2011) (stating that since 2008 Leggett & Platt had met with or sent CBP information regarding specific evidence of duty evasion on 21 separate occasions).

54 *Staff Report Regarding Duty Evasion: Harming U.S. Industry and American Workers*, Prepared for Senator Ron Wyden (Nov. 8, 2010) at 5 ("Staff Report Regarding Duty Evasion").

55 *See* USTR 2010 Report to Congress on China's WTO Compliance (Dec. 2010) at 106.

56 *Id.* at 107.

57 *Id.* at 58.

III. BECAUSE OF CHINA'S TRADE VIOLATIONS, ITS WTO ACCESSION HAS NOT BENEFITED U.S. EXPORTS OR WORKERS AS EXPECTED

A. Because China Has Largely Failed to Fulfill its WTO Obligations, the United States Has Not Realized the Expected Benefits from China's WTO Accession

As one of the largest economies in the world, China's WTO accession was expected to have significant positive economic consequences for the United States and WTO Member countries around the world. Many in the United States expected China's accession to lead to an expansion of U.S. exports to China and greater U.S. investment in China, and to create jobs in the United States. However, as discussed above, China has largely failed to live up to the commitments it made upon accession, depriving the United States and other WTO Member countries of the expected benefits, while China continues to enjoy the advantages of its WTO membership.

For example, U.S. proponents of China's WTO accession argued that it would help balance the U.S.-China trade deficit and create more U.S. jobs by increasing U.S. exports to China's large and growing consumer market. Unfortunately, this has largely failed to occur. In fact, between 2001 and 2010 – China's first decade of WTO membership – the trade deficit with China has soared. The United States trade deficit with China increased in every year since 2001, with the exception of the recession year of 2009.[58] The deficit increased from $84 billion in 2001 to $278 billion in 2010.[59] Last year, China's exports to the United States were more than four times greater in value than U.S. exports to China.[60]

Moreover, according to some estimates, the trade deficit has been responsible for eliminating or displacing 2.8 million U.S. jobs, nearly 70 percent of which were in manufacturing.[61] In total, from China's accession to the WTO in 2001 to 2010, "the increase in U.S.-China trade deficits eliminated or displaced 2,790,100 U.S. jobs," for an average of about 310,000 jobs per year.[62]

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[58] *See* Robert E. Scott, *Growing U.S. Trade Deficit with China Cost 2.8 Million Jobs Between 2001 and 2010*, Economic Policy Institute, Briefing Paper #323 (Sept. 20, 2011) at 1. "Since China entered the WTO in 2001, this deficit has increased by $19.4 billion per year, on average, or 14.2% per year." *Id.* at 7.

[59] *Id.* at 7.

[60] *Id.* at 5.

[61] *Id.* at 1.

[62] *Id.* at 8.

China's failure to abide by its WTO commitments also has had negative consequences for the global trading market as a whole. For example, China's support of its large SOEs and intervention in their commercial decisions forces U.S. and other global companies to compete directly against the Chinese government in the U.S. and global markets, creating significant imbalances that harm U.S. workers and distort the markets in favor of Chinese companies. The imposition of WTO-inconsistent export restrictions on raw materials distorts global trade in those materials, artificially lowering prices for the products within China to the advantage of Chinese producers, and lowering supply and raising prices for the rest of the world's manufacturers. Likewise, the provision of government subsidies to domestic Chinese manufacturers provides those producers with an unfair advantage in global trade.

B. The Chinese Government Retaliates Against U.S. and Other Companies who Express Legitimate Trade-Related Concerns

Not only has the United States been deprived of many of the anticipated benefits of China's WTO accession, when the U.S. government has attempted to use WTO-approved means to bring China into compliance with its obligations, it has been the target of retaliatory actions from China. Individual U.S. companies have also felt the effects of retaliatory Chinese practices. The U.S. and other world governments are often hindered in their attempts to use the WTO dispute settlement system to obtain China's compliance by their own domestic companies, who are hesitant to assist in any U.S. government case or investigation due to legitimate fears of Chinese retaliation. In a November 30, 2011 speech, U.S. Ambassador to the WTO Michael Punke noted the "perception among WTO Members that Chinese government authorities at times use intimidation as a trade tool."[63] Ambassador Punke stated that companies in WTO Member nations report that "Chinese regulatory authorities threaten to withhold necessary approvals or take other retaliatory actions against foreign enterprises if they speak out against problematic Chinese policies or are perceived as responding cooperatively to their governments' efforts to challenge them."[64]

In addition, the Chinese government has taken retaliatory actions on a larger scale, by instituting trade remedy cases in China in response to legitimate trade cases filed against Chinese

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63 *Remarks by United States Ambassador to the World Trade Organization Michael Punke on the China Transitional Review of the Protocol of Accession to the WTO Agreement,* USTR News (Nov. 30, 2011).

64 *Id.*

products abroad. As Ambassador Punke described, "{i}n recent years, a pattern also has seemed to emerge of the Chinese government's reflexive resort to trade actions in response to legitimate actions taken by the United States or other trading partners under their trade remedy laws. This type of conduct is at odds with fundamental principles of the WTO's rules-based system."[65] For example, in apparent response to AD and CVD investigations recently filed in the United States against solar cells and modules from China, the Chinese government immediately instituted its own trade remedy case to investigate subsidies to the U.S. renewable energy industries, including the solar, hydropower, and wind energy industries.[66] Such retaliatory actions can discourage legitimate trade complaints and defeat the purpose of the WTO's dispute settlement system.

IV. <u>CONCLUSION</u>

China's status as the world's second-largest economy makes its failure to live up to many of its WTO obligations – including intentionally flouting certain WTO rules and exploiting loopholes or openings in the WTO system – all the more troubling. Given its size and economic influence, China's refusal to abide by many of its WTO commitments not only harms U.S. and third country economic interests, but threatens to undermine the legitimacy of the WTO and the international rules-based trading system. Indeed, the failures of the Doha round can largely be attributed to China – many developing countries have been unwilling to reduce their tariffs, since China would be the primary beneficiary at the expense of their own industries.

To address these failures, the United States must take a more proactive approach. For instance, the United States should:

- *Aggressively litigate China's violations at the WTO*. The United States should exhibit boldness and leadership in bringing cases to the WTO. The United States should advance aggressive arguments where appropriate (i.e., on currency) and target the most pressing and systemic of problems, instead of engaging on tangential issues. To do this, USTR needs more staff and resources.
- *Stress reciprocity as a guiding principal for all trade and investment issues related to China*. For example, the United States should reassess the access of Chinese SOEs to the U.S. market and takes steps to ensure that China eliminates state support for its "go global" directive.

65 *Id.*

66 *See* Owen Fletcher, *China to Investigate U.S. Renewable Energy Policies*, The Wall Street Journal (Nov. 25, 2011).

- *Build bilateral and multilateral coalitions with trading partners to limit China's artificial advantages*. In addition to forging better commercial ties with other trading partners, the United States should seek to address the distortions caused by SOEs, export restrictions, currency manipulation and other issues in the context of the Trans-Pacific Partnership agreement, other trade agreements, and international fora.
- *Press for a new, reconfigured round of WTO negotiations*. The new round would be premised in large part on eliminating the loopholes in the existing system that China has used to its advantage. Because China is unlikely to be a willing participant in such negotiations, the United States would likely have to achieve some success with respect to the aforementioned approaches in order to bring China to the negotiation table.

In short, what is needed is a bold, concerted and coordinated effort by the U.S. Congress and Executive branch to send a clear signal to China that it must end its trade-distorting policies and practices and comply with all of its WTO obligations.