

China's Compliance with the World Trade Organization and International Trade Rules

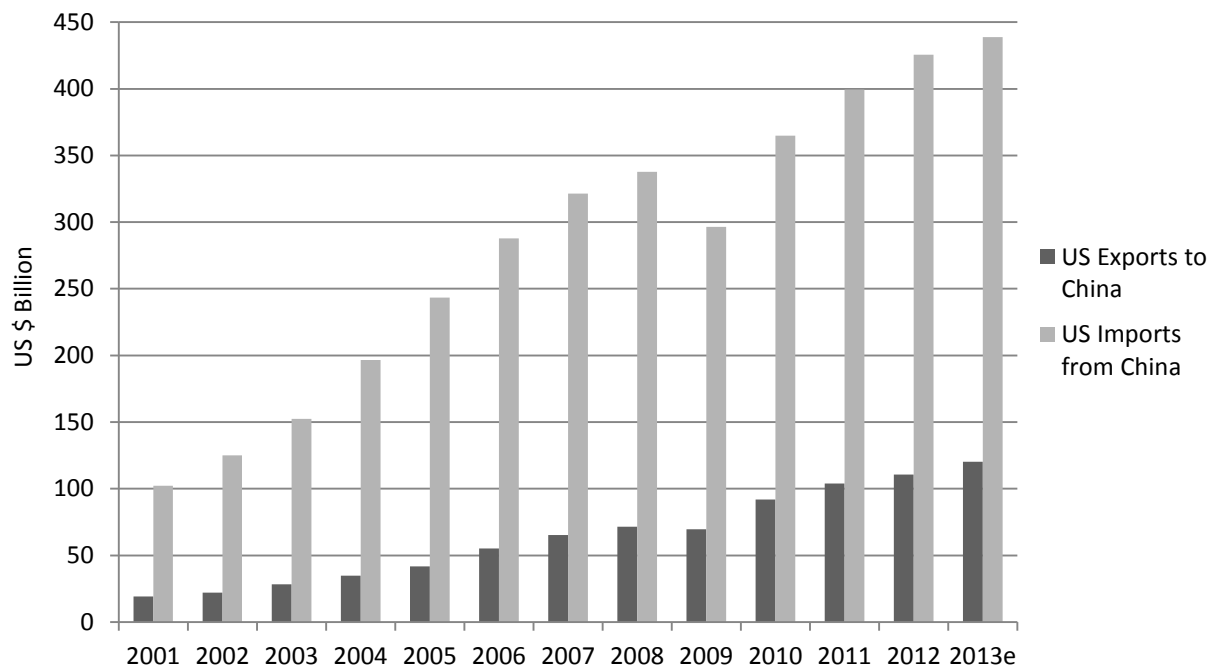
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I. Introduction

Since China joined the WTO twelve years ago, it has become the world's number one exporter and the most important U.S. trading partner. Unfortunately, the growth in trade between the U.S. and China has not been balanced. While annual U.S. exports to China grew by \$101 billion from 2001 to 2013, annual U.S. imports from China rose by nearly \$337 billion, more than three times as much.² As a result, our trade deficit with China has nearly quadrupled since 2001. Even though China only accounted for eight percent of our exports to the world in 2013, it accounted for 19 percent of our imports and a full 46 percent of our trade deficit.³



¹ Partner, Law Offices of Stewart and Stewart. This testimony is submitted in the author's personal capacity and not on behalf of the firm or its clients.

² Import and export statistics are from USITC Dataweb. Imports are general imports; exports are total exports. Imports and exports for 2013 estimated based on first eleven months of data.

³ *Id.*

Though China has reaped significant benefits from its accession to the WTO, it continues to violate many of its WTO obligations both on paper and in practice. Despite the rapid ascent of China as a major trading nation, the Government of China has failed to assume the responsibility and leadership necessary to fulfill its obligations as a Member of the WTO. WTO-inconsistent policies that China continues to pursue twelve years after accession include discrimination against foreign goods and firms, localization requirements, prohibited export subsidies and other massive trade-distorting subsidies, export restraints, and the abuse of trade remedies not as a legitimate means of correcting unfair trade but as a tool of retaliation and intimidation. These policies give Chinese producers and exporters a significant competitive advantage at the expense of producers and workers in the U.S., distort trade flows and competition, thwart innovation, and undermine the rules-based trading system.

While USTR and the Administration have made impressive efforts to identify and redress such violations, more can be done. In order to tackle these violations, particularly in the context of a Chinese legal system that is not uniformly transparent, USTR needs more resources so it can expand and intensify its excellent work. These resources are a smart investment in our country's long-term competitiveness. For the price of additional attorneys and experts at USTR, we can do more to address tens of billions of dollars of WTO-illegal subsidies, blatant discrimination by Chinese entities, and a growing trade deficit that saps U.S. production, investment, and jobs. Indeed, the important victories the U.S. has already won at the WTO when it has challenged China's policies confirm how essential U.S. leadership is in holding China accountable to the rules it has agreed to. We made significant concessions when China joined the WTO; in return, it agreed to abide by the rules. Yet if the rules are not fully and effectively enforced, the sacrifices we made when China joined the WTO will have been in vain.

USTR recently reported on the broad array of areas in which China has continued to fall short of its WTO commitments, including in areas such as intellectual property rights protection, access for investors and service providers, and transparency. This testimony highlights just four areas in which China is failing to comply with its WTO commitments. These are among the areas in which I believe U.S. industry and workers would have the most to gain from greater enforcement efforts by the U.S. They are: 1) billions of dollars in prohibited export subsidies provided by the Export-Import Bank of China and the China Development Bank; 2) discrimination by state-owned enterprises against U.S. producers and products; 3) the imposition of technology transfer, local content, and export requirements on companies investing in China; and 4) trade-distorting subsidies being provided to China's Strategic and Emerging Industries.

Finally, China's undervaluation of its currency also gives Chinese exports a significant unfair advantage and directly harms U.S. producers and workers. The U.S. should consider all available options for addressing this distortion, including options at the IMF and WTO as well as action under our trade remedy laws. These written comments are, however, limited to the four areas listed above.

II. Selected Examples of China's Non-Compliance with its WTO Commitments

A. Prohibited Export Credit Subsidies

Article 3 of the WTO Agreement on Subsidies and Countervailing Measures prohibits WTO Members from providing subsidies that are contingent, in law or in fact, whether solely or as one of several other conditions, upon export performance.⁴ China committed to eliminate all

⁴ Agreement on Subsidies and Countervailing Measures (SCM Agreement), Article 3.

such prohibited export subsidies when it joined the WTO.⁵ There is a safe harbor from this prohibition on export subsidies for official export credits, but only if those export credits comply with the terms of the *OECD Arrangement on Export Credits*.⁶ Export credits that do not comply with the terms of the *OECD Arrangement* are prohibited under WTO rules. Though China has been invited to join the *OECD Arrangement*, it has declined to do so. And, even though China is now the world's largest provider of export credits by far, it appears to be routinely flouting the terms of the *OECD Arrangement*, significantly undermining its relevance and posing a substantial threat to the competitiveness of U.S. exporters and their workers.

In 2012, the U.S. ExIm Bank estimates that the Export-Import Bank of China (China ExIm) issued \$45 billion in new medium- and long-term export credits, almost one-and-a-half times the value of such credits newly issued by the U.S. ExIm Bank in 2012.⁷ An additional \$50 billion in export credits is estimated to have been provided by the China Development Bank.⁸ In all, China provided over \$3 in export credits to Chinese firms for every dollar provided by the U.S. to its exporters.

China ExIm explains that the purpose of its programs is to support the export of Chinese products and improve their competitiveness in the international market, and it describes the export seller's credit as a loan with large amount, long maturity, and preferential interest rate.⁹

While China ExIm reveals little information about the rates that are charged under these

⁵ *Protocol on the Accession of the People's Republic of China*, WT/L/432 (Nov. 10, 2011) at ¶ 10.3; see also *Report of the Working Party on the Accession of China*, WT/MIN(01)/3 (Nov. 10, 2011) at ¶¶ 167-168.

⁶ SCM Agreement, Annex I, item (k).

⁷ Export-Import Bank of the United States, *Report to the U.S. Congress on Export Credit Competition and the Export-Import Bank of the United States* (June 2013) at 18.

⁸ *Id.* at 143.

⁹ See The Export-Import Bank of China, "Introduction;" The Export-Import Bank of China, "Export Seller's Credit."

programs, there are various second-hand reports indicating that the terms of this financing are highly concessional, with some sources citing rates as low as two, one, or zero percent.¹⁰ This information has led the U.S. ExIm Bank to conclude that China's export financing does not comply in practice with the terms of the *OECD Arrangement*.¹¹

To bring a successful WTO challenge to these subsidy programs, the U.S. must make out a *prima facie* case that the Chinese government provides export financing, that the financing is contingent on export performance, and that the rates at which the financing is provided are below market rates. Each of these elements seems relatively straightforward to establish based on publicly available information. While there is little transparency regarding the rates at which much of China's export credits are provided, the People's Bank of China does put out regular circulars indicating that at least one category of export credits, for high- and new-technology products, is subject to a rate that is lower than the Bank's own benchmark rate for "commercial" loans. According the China ExIm, such high- and new-tech products account for more than a third of their export sellers' credit disbursements.¹² Once this *prima facie* case is made, the burden would shift to China to come forward with sufficient information and argument to demonstrate that its export credits nonetheless comply with the terms of the *OECD Arrangement* and are thus not prohibited under WTO rules.

Instead of mounting a WTO challenge to China's export credits, the U.S. has instead opted to pursue negotiations with China to regulate its export financing activities. Rather than

¹⁰ See, e.g., Ryan J. Orr and Jeremy R. Kennedy, "Highlights of recent trends in global infrastructure: new players and revised game rules," *Transnational Corporations*, Vol. 17, No. 1 (April 2008) at 108-109; Deborah Brautigam, *China's African Aid: Transatlantic Challenges*, the German Marshall Fund of the United States (April 2008) at 25-26. See also Terence P. Stewart, et al., *China's Support Programs for Automobiles and Auto Parts under the 12th Five-Year Plan* (Jan. 2012) at 60.

¹¹ Export-Import Bank of the United States, *Report to the U.S. Congress on Export Credit Competition and the Export-Import Bank of the United States* (June 2013) at 18.

¹² China ExIm 2012 Annual Report at 15.

seeking China's accession to the *OECD Arrangement*, however, the U.S. is negotiating with China to agree to "international guidelines" for official export credits that, while "consistent with international best practices," also "tak[e] into account varying national interests and situations."¹³ The description of the negotiations raises concerns that China is seeking to avoid a WTO dispute by agreeing to guidelines that fall short of the requirements of the *OECD Arrangement*, which would be a significant step backward from the rules that have governed export financing for decades.

Yet even the modest goals of the negotiations may be too ambitious for the U.S. and China to meet. While the negotiations originally intended to result in agreement by 2014, no final agreement has been announced to date. Moreover, the most recent public statements regarding the negotiations suggest that any agreement may be limited to certain sectoral guidelines, and not result in a universal set of rules covering all export financing activity. In July of this year, the U.S. and China explained that negotiations had begun in earnest on guidelines for the ships and medical equipment sectors, and that such a sectoral agreement was hoped for by 2014.¹⁴ While it is unknown how much medical equipment is supported by China's export financing, ships account for less than 11 percent of China's export sellers' credit disbursements in 2012.¹⁵

Moreover, in the midst of these negotiations, the Government of China has repeatedly denied officials from the U.S. Department of Commerce the ability to verify the amounts of export financing benefitting Chinese producers in the context of countervailing duty

¹³ U.S. Department of the Treasury, "Joint U.S.-China Economic Track Fact Sheet - Fourth Meeting of the U.S. China Strategic and Economic Dialogue (S&ED)," (May 4, 2012).

¹⁴ U.S. Department of the Treasury, "Joint U.S.-China Economic Track Fact Sheet – Fifth Meeting of the U.S.-China Strategic and Economic Dialogue" (July 12, 2013).

¹⁵ China ExIm 2012 Annual Report at 15.

investigations on imports from China on an array of products, including solar cells, wind towers, and shrimp.¹⁶ In one such instance, when Commerce officials asked if they could query China ExIm’s loan database (a standard practice to verify the extent of government subsidies), China ExIm officials refused, stating they could not permit Commerce to view the database, that Commerce “should trust them” in this matter, and that it would be “nonsense” for Commerce to view the database if they did not trust their statements.¹⁷

Absent greater cooperation and transparency from China regarding its export financing programs, the U.S. should not hesitate to challenge these prohibited export subsidies at the WTO. China is already bound by WTO rules that prohibit export credits that do not comply with *OECD Arrangement*, and permitting China to provide ever greater sums of export subsidies in defiance of these rules serves only to further undermine U.S. competitiveness and, as a result, production, investment, and jobs here in the U.S.

B. Discrimination by State-Owned Enterprises

State-owned enterprises (SOEs) have had, and continue to have, a dominant presence in the Chinese market, and the Government of China has professed a policy of strengthening political control of SOEs and consolidating their position in key sectors. During the negotiation of China’s accession to the WTO, Members voiced their concerns regarding the role of the Chinese Government in the decisions and activities of SOEs,¹⁸ and China agreed to a number of important disciplines on their SOEs as a result.

¹⁶ See Memorandum from Mark Hoadley, Program Manager, AD/CVD Operations, Office 6, “Countervailing Duty Investigation of Crystalline Silicon Photovoltaic Cells, Whether or Not Assembled Into Modules, From the People’s Republic of China: Verification of the Questionnaire Responses Submitted by the Government of China” (Aug. 15, 2012) at 16.

¹⁷ *Id.*

¹⁸ *Report of the Working Party on the Accession of China*, WT/MIN(01)/3 (Nov. 10, 2011) at ¶ 44.

Article III:4 of the GATT prohibits discriminatory treatment of imported goods – while there is a limited carve-out to this obligation for government purchases of goods for governmental purposes, the exception does not apply when SOEs procure goods for commercial purposes. Nor is there any exemption for SOEs outside of the purchasing context, such as in their negotiation of joint venture agreements. National treatment obligations in the GATS have a similar scope, though they only apply to sectors in which Members have made positive commitments.

China made additional, specific commitments to respect the principle of non-discrimination in SOE purchasing decisions. In its Protocol of Accession and accompanying Working Party Report, China agreed that SOEs shall make purchases based solely on commercial considerations, that foreign enterprises will have an adequate opportunity to compete for such contracts on a non-discriminatory basis, that China will not influence, directly or indirectly, the purchasing decisions of SOEs, and that SOEs' commercial purchases will not be subject to government procurement exceptions.¹⁹ These commitments apply to purchases of both goods and services, and they appear to require non-discrimination not only for imports but also for foreign-invested firms in China.

China appears to be in violation of these important commitments. In the telecommunications sector, for example, China's big three state-owned operators reportedly purchase under a government directive to buy domestic components and equipment.²⁰ The government's policy is reflected in the telecom operators' discussion of their purchasing arrangements. China Unicom, for example, purchases equipment through contracts with its

¹⁹ *Report of the Working Party on the Accession of China*, WT/MIN(01)/3 (Nov. 10, 2011) at paras. 46, 47, 342; *Accession of the People's Republic of China*, WT/L/432 (Nov. 23, 2011) at Sec. 1(2).

²⁰ USTR, *2011 National Trade Estimate Report on Foreign Trade Barriers* (March 2011) at 64.

state-owned parent, and it warns investors that the arrangement may not be in the best interests of shareholders.²¹ Under the arrangement, the state-owned parent gets three percent of the contract cost for purchases of domestic equipment but only one percent of the contract cost for imported equipment,²² creating an incentive for the parent company to procure equipment from domestic producers even if it is more expensive than imported equipment.

Discrimination also appears in the form of domestic content and localization provisions in Chinese SOEs' sourcing and joint venture contracts. In the wind-energy sector, for example, the state-owned producer Sinovel contracted to purchase wind turbine components from American Superconductor for delivery from 2009 to 2011. The contract set out a "localization schedule" under which converters which American Superconductor had produced with foreign material would instead be produced with Chinese materials.²³ By 2010, American Superconductor reported that it had successfully localized the supply of components for its converters to China.²⁴ More recently, as part of an agreement to establish a joint-venture with a Chinese SOE to produce trucks in China, Daimler similarly agreed to "localize" the production of the truck engines to China.²⁵

The U.S. and other countries expended significant negotiating effort and bargaining capital to secure accession commitments from China regarding SOEs that go above and beyond the rules in the WTO Agreements. The U.S. has continued to press China to honor these commitments, and obtained promises of compliance in the context of the Strategic and Economic

²¹ China Unicom 2008 Form 20-F at 10.

²² China Unicom 2009 Form 20-F at 83.

²³ American Superconductor Corp. Form 8-K (June 5, 2008) at Ex. 10.1.

²⁴ American Superconductor Corp. Form 10-Q (Aug. 5, 2010) at 18.

²⁵ "Germany's Daimler to Make Trucks in China," *Agence France Presse* (Sept. 26, 2011); "Final Approval Issued by Chinese Authorities: Way Clear for Daimler's Truck Joint Venture with Foton," Daimler.com (Sept. 26, 2011).

Dialogue and other fora.²⁶ Yet, after twelve years and substantial evidence that these commitments have not been honored, there has been no formal challenge to enforce the obligations that China undertook. This lack of formal enforcement is particularly problematic given current efforts to build upon these SOE disciplines in new trade and investment agreements. While new and stronger rules are certainly needed, the U.S. must also send a strong signal that the existing rules will be effectively enforced.

C. Technology Transfer and Other Investment Conditions

As part of its accession to the WTO, China committed to be bound by the obligations contained in the Agreement on Trade-Related Investment Measures (TRIMs Agreement). Pursuant to Article 2 of the TRIMs, Members shall not apply any trade-related investment measure that is inconsistent with the national treatment obligation or the elimination of quantitative restrictions obligation contained in Articles III and XI, respectively, of the GATT.²⁷ The Annex to this provision provides an illustrative list of trade-related investment measures that would be inconsistent with Article 2, including measures that require an entity to purchase or use domestic products or that limit an entity's importation, purchase, or use of imported products based on the amount of the entity's exports.²⁸ In addition to complying with TRIMs, China also committed in its Accession Protocol to, "eliminate and cease to enforce trade and foreign exchange balancing requirements, local content and export or performance requirements made effective through laws, regulations or other measures."²⁹ Moreover, China agreed not to enforce

²⁶ See, e.g., USTR, *2013 Report to Congress on China's WTO Compliance* (Dec. 2013) at 70-71.

²⁷ Agreement on Trade-Related Investment Measures Art. 2.1.

²⁸ *Id.*, Annex ¶ 1.

²⁹ *Protocol on the Accession of the People's Republic of China*, WT/L/432 (Nov. 10, 2011) at ¶ 7.3.

provisions of contracts imposing such requirements.³⁰ China also agreed to ensure that any means for approving investments in China not be conditioned on: “whether competing domestic suppliers of such products exist; or performance requirements of any kind, such as local content, offsets, the transfer of technology, export performance or the conduct of research and development in China.”³¹

While China has revised or eliminated some measures to conform with these obligations, measures continue to remain in place that impose—whether through formal requirements or “encouragement”—local content and export requirements, as well as technology transfer and research and development requirements. As explained in the *2013 National Trade Estimate Report on Foreign Trade Barriers*:

some laws and regulations ‘encourage’ exportation or the use of local content. Moreover, according to U.S. companies, some Chinese government officials, even in the absence of applicable language in a law, regulation or agency rule, still consider factors such as export performance and local content when deciding whether to approve an investment or to recommend approval of a loan from a Chinese policy bank³²

Although such measures are inconsistent with China’s WTO obligations, policies tying foreign investment to export performance, local content, technology transfer, and research and development investments appear to continue to be present in a variety of industries throughout China.

For example, a foreign tire company that started producing in China in 2008 was required by its business license to commit to export all of its production for the first five years of its

³⁰ *Id.*

³¹ *Id.*

³² USTR, *2013 National Trade Estimate Report on Foreign Trade Barriers* at 91.

operation.³³ Additionally, the *Catalogue Guiding Foreign Investment in Industry*, with the most recent update entering into force in January 2012, lists industries that are encouraged, restricted, or permitted.³⁴ As explained in the most recent WTO Trade Policy Review of China, “[f]oreign investment in the restricted category may be permitted, subject to approval, if export sales are over 70% of total sales of the product.”³⁵ Industries listed in the most recent catalogue as “restricted” include, *inter alia*, chemical raw material products manufacturing, non-ferrous metal smelting and rolling processing, and common and special purpose equipment manufacturing.³⁶ The U.S. has exerted substantial efforts to obtain revisions to the Catalogue and other measures that restrict investment and thus provide leverage to obtain export and local content commitments, as well as other commitments from investors.³⁷ However, in its most recent report on China’s WTO compliance, USTR notes its disappointment that China has not always been responsive to these efforts.³⁸

Moreover, as noted in *The President’s 2013 Trade Policy Agenda*, the United States and other WTO Members have “continually reported that some Chinese government officials, who typically retain a high degree of discretion when reviewing investment applications, still considered factors such as technology transfer and local content when reviewing investment applications.”³⁹ In the area of technology transfer, for example, such violations continue to

³³ U.S. International Trade Commission, *Certain Passenger Vehicle and Light Truck Tires from China*, Inv. No. TA-421-7, USITC Pub. 4085 (July 2009) at 34, n.190.

³⁴ See Trade Policy Review Body, *Trade Policy Review Report by the Secretariat China*, WT/TPR/S/26/Rev.1 (July 20, 2012) at ¶ 45.

³⁵ *Id.* at ¶ 48.

³⁶ *Catalogue for the Guidance of Foreign Investment Industries* (amended in 2011), available at <http://english.mofcom.gov.cn/article/policyrelease/aaa/201203/20120308027837.shtml>.

³⁷ USTR, *2013 Report to Congress on China’s WTO Compliance* (Dec. 2013) at 80-81.

³⁸ *Id.* at 81.

³⁹ U.S. Trade Representative, *The President’s 2013 Trade Policy Agenda* at 27.

persist due to provisions in Chinese law and regulations that require that any technology provided by a foreign investor as part of a joint venture agreement be “advanced” and be appropriate to help the venture compete (including internationally);⁴⁰ furthermore, all such technology transfer agreements must be submitted for government approval.⁴¹ Various foreign firms have been subject to localization or technology transfer requirements in order to be able to invest in China and/or sell to Chinese firms (particularly state-owned firms, as noted in Section II.B, above).

The automotive sector is one sector where these types of investment conditions are evident. For example, China waives requirements that foreign investors seeking to produce complete automobiles must enter into joint ventures with majority Chinese ownership if the venture is located in an export processing zone.⁴² China has also used investment approval measures to access technology for new energy vehicles (NEVs). In March 2011, the National Development and Reform Commission issued a draft *Catalogue Guiding Foreign Investment in Industry* that proposed a new limitation on foreign ownership in NEV parts manufacturing facilities in China to no more than 50 percent.⁴³ After repeated efforts by the U.S., China removed the 50 percent limit for almost all of the key components of NEVs in the final version issued in January 2012, but retained the restriction on NEV batteries.⁴⁴ This is a significant limitation on foreign ownership in the NEV industry, because batteries are one of the critical components of most NEVs. By requiring foreign investors to partner with domestic firms, and

⁴⁰ Regulations for the Implementation of the Law on Sino-Foreign Equity Ventures, art. 41 (July 22, 2001).

⁴¹ *Id.* at Arts. 3-4.

⁴² *Policy on Development of Auto Industry* (May 21, 2004) at Article 49.

⁴³ See USTR, *2013 National Trade Estimate Report on Foreign Trade Barriers* at 69. See also USTR, *2013 Report to Congress on China's WTO Compliance* (Dec. 2013) at 83-84.

⁴⁴ *Id.*

by requiring domestic firms to have “mastery” over the technology involved in such ventures, China ensures that any foreign investor in the critical technology will be sharing that technology with its Chinese joint venture partner. USTR notes that it remains difficult to assess the extent to which China has implemented the commitments it made to comply with its WTO commitments in the NEV sector as far back as 2011.⁴⁵

Despite repeated requests from the U.S. to eliminate these WTO-inconsistent policies, and repeated assurances from China that such measures are not enforced, USTR continues to express its concern that investment approvals in China are conditioned on export performance, local content, technology transfer and research and development investment requirements. All such requirements are explicitly prohibited under terms the U.S. negotiated with China when it joined the WTO. While some requirements appear to be imposed on an *ad hoc* or informal basis, others are based in the provisions of Chinese law and policies, and form a sufficient basis for challenge at the WTO. The U.S. should work to develop the facts and arguments necessary to challenge these harmful policies at the WTO and bring China into compliance with its commitments.

D. Subsidies to Strategic and Emerging Industries

When China joined the WTO, it agreed not only to eliminate prohibited subsidies such as export subsidies, but also to be subject to WTO rules which make subsidies which are not prohibited actionable if they cause serious prejudice to another Member. When a government makes a financial contribution that is specific to an industry or region, and that contribution confers a benefit, WTO rules permit other Members to challenge those subsidies if they displace their exports, cause lost sales, suppress or depress prices, or increase the subsidizing country’s

⁴⁵ USTR, *2013 Report to Congress on China’s WTO Compliance* (Dec. 2013) at 83.

share of world trade in the subsidized good. Since 2006, the U.S. has investigated hundreds of subsidy programs benefitting dozens of goods exported from China to the U.S., including, among others, reduced tax rates for companies in preferred industries and regions,^{46 47} preferential policy lending from state-owned banks at below market rates at the central and provincial levels,⁴⁸ the provision of electricity and key raw materials by SOEs for less than adequate remuneration (LTAR),^{49 50} the provision of land by central and local governments for LTAR,⁵¹ and numerous grant programs.⁵² In response to the lack of transparency in China regarding the broad array of subsidy programs it maintains, as well as its failure to notify the WTO of these programs as required by WTO rules, in 2011 the U.S. submitted a counter subsidy notification to the WTO that covers hundreds of subsidy programs at the central and sub-central levels of the Chinese government.⁵³ These include export subsidies and domestic content subsidies, as well as other injurious subsidies.⁵⁴ More than two years later, action to eliminate these subsidies still has not occurred.

⁴⁶ *Light-Walled Rectangular Pipe and Tube From the People's Republic of China: Final Results of the Expedited First Sunset Review of the Countervailing Duty Order*, 78 Fed. Reg. 48416 (Dep't Comm. Aug. 8, 2013), and accompanying Issues and Decision Memorandum at 6.

⁴⁷ *Certain Kitchen Appliance Shelving and Racks From the People's Republic of China: Final Results of Countervailing Duty Administrative Review; 2010*, 78 Fed. Reg. 21594 (Dep't Comm. Apr. 11, 2013) and accompanying Issues and Decision Memorandum ("KASR IDM") at 7-8.

⁴⁸ *Drill Pipe From the People's Republic of China: Final Results of Countervailing Duty Administrative Review; 2011*, 78 Fed. Reg. 47275 (Dep't Comm. Aug. 5, 2013) and accompanying Issues and Decision Memorandum at 11-13.

⁴⁹ *Id.* at 13-14.

⁵⁰ KASR IDM at 9-12.

⁵¹ *Drawn Stainless Steel Sinks From the People's Republic of China: Final Affirmative Countervailing Duty Determination*, 78 Fed. Reg. 13017 (Dep't Comm. Feb. 26, 2013) and accompanying Issues and Decision Memorandum ("Steel Stinks IDM") at 22-24.

⁵² KASR IDM at 13-14, 15; Steel Stinks IDM at 25-28.

⁵³ *See Subsidies—Request from the United States to China Pursuant to Article 25.10 of the Agreement, G/SCM/Q2/CHN/42* (Oct. 11, 2011).

⁵⁴ *See id.*

To date, however, the U.S. has only challenged prohibited subsidies provided by China at the WTO – it has not taken any action to challenge non-prohibited subsidies that are nonetheless causing harm to American industries and workers both in the U.S. market and abroad. Instead, industries seeking relief from such subsidy programs must file a countervailing duty case and seek import duties to offset those subsidies; even if relief is obtained, it only covers competition in the U.S. market, not in China or third-country markets. While disputes challenging actionable subsidies are fact-intensive and thus complicated to pursue, providing companies and workers with only partial relief through the domestic trade remedy system imposes major long term costs on our ability to compete.

This ability to compete is particularly threatened in the seven “Strategic and Emerging Industries” (SEIs) in which China plans to invest a reported \$1.5 trillion dollars over the coming years. China’s 12th Five-Year Plan for National Economic and Social Development (2011-2015) identifies seven priority SEIs and aims to increase their contribution to GDP from the current 2 percent level to 8 percent by 2015 and 15 percent by 2020.⁵⁵ Achieving this goal would require the sectors to grow more than seven times over in size over less than a decade – a massive undertaking that could likely not be achieved without displacing foreign competitors from the market. Indeed, the Government of China’s explicit goal is to displace global competitors in each of the seven sectors; it aims to become a global leader in each of these industries by 2030.⁵⁶

The seven SEIs are key industries that many countries will be hoping to pursue in the coming years: (1) energy saving and environmental protection; (2) new generation of

⁵⁵ China’s 12th Five-Year Plan for National Economic and Social Development at Chapter 10, translation available at <http://www.britishchamber.cn/content/chinas-twelfth-five-year-plan-2011-2015-full-english-version>.

⁵⁶ *Emerging Strategic Industries: Aggressive Growth Targets*, China Strategy, HSBC Global Research (October 19, 2010).

information technology; (3) biotechnology; (4) high-end equipment manufacturing; (5) new energy; (6) new materials; (7) new energy vehicles.⁵⁷ China's State Council first identified these industries in its Decision on Accelerating the Fostering and Development of New Strategic Industries announced in 2010. China will provide SEIs with preferential policies, incentives, and funds that media reports indicate could reach \$1.5 trillion from 2011 to 2015.⁵⁸

In 2012, China issued three catalogues on SEIs development. Among these, the Development Priorities of Key Generic Technologies and Key Products in Strategic Emerging Industries issued by MIIT in July 2012 stands out because it identifies major research and development units and major companies, as well as government policies and funds designed to spur development in each category. However, only a small number of companies listed have any foreign investment, as the list heavily favors Chinese-invested firms, particularly state-owned enterprises and national champions.⁵⁹ MIIT further suggested that another catalogue should be used by other Chinese government departments to "issue targeted supporting fiscal and taxation policies."⁶⁰

The Chinese government has decided to dedicate a tremendous amount of resources to help these industries develop and overtake global competitors. If China succeeds, it will be because the subsidies it provides to these industries enable them to take market share from other producers, including industries in the U.S. The U.S. is closely following the SEI program, and it

⁵⁷ China's 12th Five-Year Plan for National Economic and Social Development at Chapter 10, translation available at <http://www.britishchamber.cn/content/chinas-twelfth-five-year-plan-2011-2015-full-english-version>.

⁵⁸ See Ping Gong and Jessica Wang, *China's 12th Five-Year Plan: An Overview* (May 18, 2011).

⁵⁹ USTR, *2013 National Trade Estimate Report on Foreign Trade Barriers* at 98.

⁶⁰ *Id.*

has urged China to be more transparent about subsidies provided to these industries.⁶¹ As part of this monitoring, the U.S. should ensure that any negative impact the SEI policy does have on U.S. producers and workers is quickly and effectively redressed, including through WTO dispute settlement if merited.

III. Conclusion

Holding China accountable to its WTO commitments should be one of the very top trade priorities of the U.S. government. China is our largest trading partner, and continued violations by China distort trade and investment, contribute to a growing trade deficit, harm U.S. producers and workers, and undermine innovation. USTR has made significant strides in its China enforcement efforts in recent years, and those efforts are paying off in successful WTO dispute settlement outcomes and negotiated commitments obtained bilaterally from China. As China's role in the world trading system continues to grow, however, its responsible compliance with the rules of the road remains sorely lacking. In the four areas identified in this testimony, there appear to be meritorious WTO disputes that would affect billions of dollars in subsidies, the development and safeguarding of critical technologies, and industries that support thousands of American jobs. Additional enforcement resources and intensified enforcement efforts would deliver significant benefits to U.S. firms, workers, and communities.

⁶¹ USTR, *2013 Report to Congress on China's WTO Compliance* (Dec. 2013) at 46-47.