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David Spooner
Assistant Secretary for Import Administration
U.S. Department of Commerce
Central Records Unit, Room 1870
Pennsylvania Avenue and 14th Street, N.W.
Washington, D.C. 20230

Re: Antidumping Methodologies in Proceedings Involving Certain Non-Market Economies: Market-Oriented Enterprise

Dear Assistant Secretary Spooner:

On behalf of United States Steel Corporation ("U.S. Steel"), we hereby respond to the October 25, 2007 request for comments issued by the Department of Commerce (the "Department") on whether it should consider granting market-economy treatment to individual enterprises in antidumping proceedings involving the People's Republic of China ("China").[1] The Department has specifically asked parties to address: (1) whether there is a legal basis for a market-oriented enterprise ("MOE") test; (2) whether it is administratively feasible to identify an MOE operating within a broader non-market economy ("NME") environment; (3) whether the

[1] *Antidumping Methodologies in Proceedings Involving Certain Non-Market Economies: Market-Oriented Enterprise*, 72 Fed. Reg. 60649 (Dep't Commerce October 25, 2007) (request for comments) (the "Second Request for Comments"). Although comments in response to the Department's request were originally due no November 26, 2007, the Department extended the deadline for such comments to December 10, 2007.

Department could rely on a so-called MOE's prices and costs, particularly for the inputs of labor, land and capital; and (4) whether it is appropriate and feasible to use an enterprise's own prices and costs within China in conjunction with certain surrogate prices and costs in the Department's antidumping duty calculations.[2]

The Department should not adopt any proposal that would allow individual enterprises in antidumping proceedings involving China to be granted market-economy treatment. First, U.S. law does not contemplate an individual enterprise in an antidumping proceeding being treated as a so-called MOE. To the contrary, Congress has expressed its clear intent that the Department must use its NME antidumping methodology unless Chinese firms can show that they are part of a market-oriented industry ("MOI"). Second, at a basic conceptual level, it would be nonsensical to treat an individual Chinese enterprise as market-oriented where it could not be shown that the enterprise was part of an MOI. Third, it would not be administratively feasible to identify an MOE. Ensuring that an enterprise is so isolated from the rest of the Chinese economy that it deserves MOE status would overwhelm the Department's already constrained resources and would impose an impossible burden on petitioners seeking to disprove claims of MOE status. Fourth, the Department simply would not be able to rely on a Chinese enterprise's input prices. The valuation of labor, land, and capital inputs poses especially grave problems, and the distortions created by these three inputs permeates the rest of the Chinese economy in ways that cannot be ascertained and resolved. Finally, it would be inappropriate for the Department to use its proposed hybrid approach because the statute does not allow the Department to mix surrogate values and prices for inputs sourced from NME countries.

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[2] Id.

I. THE TREATMENT OF INDIVIDUAL CHINESE ENTERPRISES AS "MARKET-ORIENTED ENTERPRISES" IS NOT CONTEMPLATED BY U.S. LAW

The Department has asked for comment on "whether there is a legal basis for a MOE test."[3] U.S. law does not contemplate treatment of individual Chinese enterprises as MOEs. Indeed, Congress has clearly expressed its intent that the NME methodology be used except where Chinese enterprises can establish that they are part of an MOI.

Congress specifically expressed its intent regarding the use of an industry-wide test during China's accession to the WTO. In 1999, in bilateral negotiations with China regarding its accession, the U.S. and China agreed that the U.S. could apply its current NME methodology, except where industries were shown to be market-oriented.[4] One year later, when Congress authorized the President to consent to China's WTO accession, Congress unambiguously made such authority contingent on the U.S.'s continuing to apply its NME methodology unless Chinese enterprises could show they were operating within an MOI.[5] Consistent with this Congressional mandate, when consenting to China's accession to the WTO, the U.S. ensured that

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[3] Id. at 60650.

[4] See "Summary of U.S.-China Bilateral WTO Agreement," The White House Office of Public Liaison (Nov. 17, 1999) (the "U.S.-China Bilateral Summary") at 7, attached hereto as Exhibit 1; "U.S.-China WTO Deal Allows Curbs on Exports for 12 Years," Inside U.S. Trade (Nov. 16, 1999), attached hereto as Exhibit 2.

[5] Specifically, Congress mandated that, "{p}rior to making the determination" to consent to China's WTO accession, the President must certify that the terms and conditions for China's accession "are at least equivalent" to those agreed in the November 15, 1999 bilateral agreement between the U.S. and China. U.S.-China Relations Act of 2000, Pub. L. 106-286, div. B, Oct. 10, 2000, 114 Stat. 891, at § 101(b) (emphasis added). The bilateral agreement provided, in turn, that the NME methodology would be applied to Chinese enterprises unless they demonstrated that they were members of an MOI. U.S.-China Bilateral Summary at 7. Thus, Congress mandated that the U.S. would not consent to China's WTO accession without the ability to use its NME methodology subject to an MOI test only.

it could use its NME methodology with respect to Chinese enterprises unless they could "clearly show that market economy conditions prevail in the industry."[6] Finally, after China's accession, Congress made no changes to existing U.S. law, further evidencing Congress's intent to keep the status quo - i.e., for the Department to use the current NME methodology unless enterprises could pass an MOI test.

The creation and application of an MOE test would clearly violate Congress's intent. For this reason alone, the Department should not adopt an MOE test.

II. GRANTING MOE STATUS TO INDIVIDUAL CHINESE ENTERPRISES DOES NOT MAKE SENSE ON A CONCEPTUAL LEVEL

In addition to the legal preclusion addressed above, it would be nonsensical on a basic conceptual level to treat an individual Chinese enterprise as market-oriented. As established below, an individual Chinese enterprise cannot possibly disentangle itself from all of the distortions inherent within an industry that is not itself market-oriented.

This conceptual problem becomes apparent when considering how distortions in one enterprise will inevitably have a distorting impact on other enterprises within the same industry. The manner in which any individual enterprise sets its prices will be affected by the prices set by other enterprises in its industry. If other enterprises in the industry set prices as a result of direct or indirect government control, the upstream suppliers of the individual enterprise's inputs and the downstream purchasers of the enterprise's products will also be distorted. The ways in which such distortions can and do occur are countless. Two examples are provided below.

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6 Protocol on the Accession of the People's Republic of China, WT/L/432 (Nov. 23, 2001) at Art. 15(a)(i).

First, where the Chinese government directly owns even one enterprise in an industry, that industry member's influence in the market would increase dramatically. In turn, such an increase in market influence would distort both the prices that the state-owned enterprise pays for its inputs and the prices that it extracts from its customers. The distorting impact of that one enterprise would then have ripple effects on other enterprises within the same industry. Such other enterprises would ultimately pay distorted prices for their inputs and set distorted prices for their products.

Labor provides a second example. Even if the Department were to find that one Chinese enterprise negotiates its wages and benefits free from direct government control or interference, that enterprise would still be impacted by the labor environment of the overall industry. Other enterprises that are subject to government control or interference and that pay a distorted price for labor will distort the wages paid to laborers throughout the industry.[7] Thus, even though the government might not directly interfere with the wages of one particular enterprise, that one enterprise would still be paying wages that were set within the context of a labor environment influenced by government control.

The upshot of this discussion is that even if the government relinquishes control over one enterprise within an industry, its control over other enterprises will continue to have distorting effects that bleed over into the rest of the industry. An enterprise operating in a non-market oriented industry cannot avoid having its costs and prices influenced by other enterprises within

[7] See generally, B.M. Fisher & D.T. Yang, China's Labor Market (Jan. 2004) (prepared for the Conference on "China's Market Reforms" organized by Stanford Center for International Development, Stanford University, September 19-20, 2003), available at http://www.wfu.edu/~caron/ssrs/Yang.doc (discussing manner in which distortions of state-owned enterprises ripple throughout the Chinese labor market).

that same industry. Thus, it would be inappropriate – at a basic conceptual level – to grant MOE status to an enterprise that has not been shown to be operating within an MOI.

III. IT IS NOT ADMINISTRATIVELY FEASIBLE TO ATTEMPT TO IDENTIFY A MOE OPERATING WITHIN A BROADER NME ENVIRONMENT

Even assuming, *arguendo*, that there was a legal and conceptual basis for the Department to apply an MOE test, it would not be administratively feasible to do so. For this reason as well, the Department should not adopt an MOE test.

To treat an NME enterprise as if it were a market-economy enterprise, despite the fact that the economy in which it operates is non-market, all prices charged and costs incurred by the individual enterprise must be market determined. The reason for imposing this strict requirement in the antidumping context is plain. To extend market-oriented treatment to an NME enterprise and then rely on that enterprise's actual sales prices and costs, the Department must satisfy itself that those prices and costs are not distorted. Otherwise, the Department will risk making improper determinations of dumping margins.

At a microeconomic level, the Department would have to determine that there is no government involvement in the individual transactions between an enterprise and the providers of its inputs as well as between the enterprise and the purchasers of its products. Such involvement could take many forms. It could include price controls set by the national government for certain goods, as well as any price controls set at the local level.[8] Import price

[8] Memorandum from Shauna Lee-Alaia, Lawrence Norton, and Anthony Hill to David M. Spooner, Assistant Secretary for Import Administration, Regarding Antidumping Duty Investigation of Certain Lined Paper Products from the People's Republic of China – China's Status as a Non-Market Economy at 47-48 (Aug. 30, 2006) (“August 30 Memorandum”) (Public Document).

controls through the use of state trading enterprises would also have to be taken into account.[9] Even the price for common inputs such as electricity is determined by political controls, rather than the market, in an NME.[10]

The Department would be required to conduct an equally comprehensive macroeconomic inquiry as well. An inquiry into an enterprise's transactions cannot simply look at whether the individual transactions between an enterprise and its suppliers and customers are free from government involvement. Rather, the Department would have to look beyond direct state involvement in the specific transactions between the enterprise under investigation and its suppliers and customers to ascertain whether market forces are actually at work in setting prices. Indeed, the government continues to interfere with the market in ways that would not be noticed if the Department confined its inquiry to government interference in specific transactions.

For every single input purchase and product sale, the Department would have to consider all possible means of market intervention for every enterprise in the industry in determining whether just one enterprise's costs and prices are distorted. Such an analysis would require the Department to examine the transactional minutia and the entire regulatory and institutional environment regarding each input and product. Many enterprises obtain inputs from multiple sources and sell their products to many customers, and all these relationships would have to be assessed. The Department could not identify an MOE without performing such inquiries.

Finally, the Department's instituting such a test would encourage a flood of requests for MOE status. Assessing whether just one Chinese enterprise should be granted MOE status

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[9] Id. at 48.

[10] Id. at 50.

would be a gargantuan administrative task. Yet no matter how the Department defined the term "market-oriented enterprise," it can rest assured that virtually every Chinese enterprise in virtually every case thereafter would argue that it is a "market-oriented enterprise." The Department, which has serious resource constraints as it is, would be forced to spend scarce time and resources addressing each claim for MOE status and would be required to resolve such claims early in its proceedings. Petitioners would also be forced to spend vast amounts of time and money in contesting such claims, no matter how specious, in proceedings before the Department. In fact, while each enterprise would only have to address MOE status for itself, petitioners would be saddled with the burden of addressing MOE status for all the Chinese enterprises seeking it.

In sum, implementation of an MOE test would be administratively unfeasible. The Department should therefore reject any proposal for the adoption of such a test.

IV. THERE ARE NO CONDITIONS UNDER WHICH THE DEPARTMENT COULD RELY ON A SO-CALLED MOE'S PRICES AND COSTS

The Department has also asked "to what extent, and under what conditions, the Department should rely on an MOE's prices and costs, particularly for those inputs that are inextricably linked to the broader operating economic environment, *i.e.*, labor, land, and capital."[11] Labor, land, and capital inputs are fundamentally distorted by the NME environment in China, and, as a result, the Department simply may not rely on the prices and costs of an individual Chinese enterprise.

[11] Second Request for Comments, 72 Fed. Reg. at 60650.

The Department could never rely on prices for labor, land, and capital inputs. The Department's own August 30 Memorandum addresses in significant detail the multiple layers of distortions inherent within these inputs. Furthermore, labor, land, and capital will affect virtually all other inputs as well. For example, coal is a major input in the production of steel. Yet the Department could not rely on the price a Chinese steel producer paid for its coal due to the extent to which distortions in the labor used to mine the coal affected the coal's price. The Department cannot avoid the distorting impact that labor, land, and capital would have on each of the inputs used in the production of steel or, for that matter, any other product. Indeed, this fundamental problem re-emphasizes the point that extending market-oriented treatment to individual Chinese enterprises is an irremediably flawed proposal at even a basic conceptual level.

V. IT WOULD NOT BE APPROPRIATE TO USE AN ENTERPRISE'S OWN PRICES AND COSTS WITHIN CHINA IN CONJUNCTION WITH CERTAIN SURROGATE PRICES AND COSTS.

Finally, the Department has asked whether it would be appropriate and feasible to use an enterprise's own prices and costs within China in conjunction with certain surrogate prices and costs in its antidumping duty calculations.[12] U.S. law does not permit the Department to use a hybrid methodology that combines market-economy and NME treatment in this way. Rather, Section 773(c)(1) of the Tariff Act of 1930, as amended (the "Act"), provides the Department with an "either/or" choice when calculating the normal value of NME merchandise.

Under Section 773(c)(1)(B) of the Act, if the Department finds that the "available information" does not permit use of the methodology set forth in Section 773(a), the Department "shall determine the normal value of the subject merchandise on the basis of the value of the

[12] Id.

factors of production utilized in producing the merchandise."[13] Simply put, if normal value cannot be determined pursuant to Section 773(a)'s market-economy methodology, then Section 773(c)'s NME methodology must be used and normal value must be based on the value of the factors of production used in producing the merchandise under consideration.

The question then becomes, in determining the value of the factors of production for an NME enterprise, can the Department rely on prices actually paid for inputs the enterprise sourced from the NME country? Section 773(c) precludes such reliance, providing that:

> {T}he valuation of the factors of production shall be based on the best available information regarding the values of such factors in a market economy country or countries considered to be appropriate by the administering authority.[14]

In other words, the statute unambiguously states that the factors of production must be valued using information from market-economy countries. It does not allow the Department to rely on the prices paid for inputs sourced from the NME country.[15]

Section 773(c) of the Act simply does not provide the Department the discretion to combine surrogate country values with NME input costs in determining normal value. Thus, it would be inappropriate and, in fact, unlawful for the Department to use an enterprise's own

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[13] 19 U.S.C. § 1677b(c)(1) (2000) (emphasis added).

[14] Id. (emphasis added).

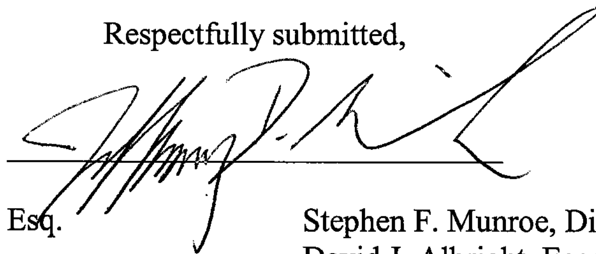
[15] The decision in Lasko Metal Products, Inc. v. United States is consistent with this principle. 43 F.3d 1442, 1445 (Fed. Cir. 1994). There, the Federal Circuit held that the statute "permits the {Department} to determine the factors of production using both surrogate country values and actual cost values," but only where the Department relies on the prices that Chinese manufacturers actually pay for inputs sourced from market economies. See id. Indeed, in Magnesium Corp. of America v. United States, the Federal Circuit emphasized that its decision in Lasko was "based on 'the amount the Chinese manufacturers {under examination} had actually paid on the international market for the supplies they used.'" 166 F.3d 1364, 13 (Fed. Cir. 1999) (quoting Lasko, 43 F.3d at 1445) (emphasis in original).

prices and costs within China in conjunction with surrogate prices and costs in its antidumping duty calculations.

V. CONCLUSION

For the reasons stated above, the Department should not adopt any proposal that would allow individual enterprises in antidumping proceedings involving China to be granted market-economy treatment. Such a proposal is particularly inappropriate at this time. U.S. Trade Representative Susan C. Schwab recently expressed concern over China's "backsliding in market-oriented economic reforms" and stated that, "{i}n China, economic retrenchment seems to be taking the form of shielding China's economy from the very market forces that have allowed it to grow so rapidly."[16] Given China's "backsliding" and "economic retrenchment," it would be nonsensical for the Department to adopt any proposal allowing individual Chinese enterprises to seek market economy treatment in antidumping proceedings.

Respectfully submitted,



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[16] "Remarks by U.S. Trade Representative Susan C. Schwab at the George H.W. Bush U.S.-China Relations Conference, Washington, DC" at 14 (Oct. 23, 2007), available at http://www.ustr.gov.

EXHIBIT 1

Source: The White House Office of Public Liason
NOVEMBER 17, 1999

BRIEFING ON THE CLINTON ADMINISTRATION AGENDA FOR THE WORLD TRADE ORGANIZATION MATERIAL

SUMMARY OF U.S. - CHINA BILATERAL WTO AGREEMENT

I. AGREEMENT HIGHLIGHTS

The U.S.-China WTO agreement covers all agricultural products, all industrial goods, and all service areas.

Industrial Tariffs
China's industrial tariffs will fall from an overall average of 24.6% in 1997 to an overall average of 9.4% by 2005.

On U.S. priority industrial products, tariffs will fall to 7.1% with the majority of tariff cuts fully implemented by 2003. Tariffs will fall on a range of products including: wood, paper, chemicals, capital and medical equipment.

In information technology, tariffs on products such as computers, semiconductors, and all internet-related equipment, will fall from an average of 13.3% to 0% by 2005.

Agriculture
On U.S. priority agriculture products, tariffs will be reduced from an overall average of 31.5% to 14.5% by January 2004, at the latest.

Priority Products	Tariffs Pre-Agreement	Tariffs Post-Agreement
Beef	45	12%
Grapes	40%	13%
Wine	65%	20%
Cheese	50%	12%
Poultry	20%	10%
Pork	20%	12%
OVERALL AVERAGE	*31.5%*	*14.5%*

China will expand access for of bulk agriculture commodities, on products including corn, cotton, wheat, rice, barely, soybean oil.

China will eliminate export subsidies -- this is especially critical for U.S. cotton and rice producers.

China will for the first time ever permit private trade (trade between private parties) in agriculture.

Services
On industrial goods, China will for the first time permit the right to import and export without middle-men -- so-called trading rights -- as well as full rights of distribution including wholesale and retail and aftersale service, repair, maintenance, and transport.

The telecommunications, insurance, banking, securities, audio visual, and professional service sectors, to name a few, will all have expanded market access under the agreement.

II. RESOLUTION OF KEY UNRESOLVED ISSUES

- Import Surge Mechanism. China has agreed to a special safeguard mechanism that will remain in place for 12 years following accession and that can be used to address rapid increases in imports from China that cause or threaten market disruption.

- Anti-Dumping. The agreement ensures that the United States can continue to apply our current non-market economy methodology in antidumping cases involving imports from China for 15 years. China can, of course, request review under U.S. law of specific sectors or the economy as a whole to determine if it is market oriented and no longer subject to the special methodology.

- Motion Pictures. A previously unresolved issue had been the degree to which China restricted imports of films. Prior to the agreement, China permitted a maximum of 10 foreign films. Under the agreement, China will quadruple imports to 40 films after accession, growing to 50 films in three Years, of which 20 will be on a revenue-sharing basis, in each of the three Years.

- Internet Access. Because of the enormous projected growth in internet access in China over the coming decade, a key priority of the U.S. was to ensure that China's telecom service commitment clearly included all aspects of internet service. The agreement ensures that Internet services will be liberalized at the same rate as other key telecommunications services.

- Satellites. China has clarified that it will permit provision of telecommunications services via satellite.

- Auto Financing. China has now made commitments for non-bank foreign financial institutions to be able to provide auto financing upon China's accession. This in combination with commitments regarding importation, distribution, sale, financing, and maintenance and repair of automobiles will help open up this key sector for U.S. industry.

- Accelerated Auto Tariff Reduction. As part of the efforts to find "win-win" solutions to sensitive areas, China agreed to accelerated tariff reduction in exchange for a slightly longer phase-in period. This provides earlier market access with auto tariffs still being reduced from the current 100-80 percent to 25 percent by July 1, 2006.

- Telecommunications. While the United States agreed to China's request to limit foreign equity participation in value-added and paging services to 50 percent, China agreed to both accelerate significantly the percentage of equity participation in the first two years and eliminate geographic restrictions on an accelerated basis. China had indicated it would allow 35% foreign ownership for value-added and paging services two years after accession and 51% four years after accession. China will now allow 49% foreign ownership in the first year of accession and 50% foreign ownership in the second year.

- Life Insurance. While the United States agreed to China's request to limit foreign equity participation in life insurance to 50%, China agreed to significantly accelerate the elimination of geographic restrictions the percentage of equity participation in the first few years.

SUMMARY OF U.S. - CHINA BILATERAL WTO AGREEMENT

AGRICULTURE

The Agreement provides increased access for U.S. exports across a broad range of commodities and elimination of barriers. Commitments include:

- Significant cuts in tariffs that will be completed by January 2004. Overall average for agricultural products will be 17 percent and for U.S. priority products 14.5 percent.

- Establishment of a tariff-rate quota system for imports of bulk commodities, e.g., wheat, corn, cotton, barley, and rice, that provides a share of the TRQ for private traders. Specific rules on how the TRQ will operate and increased transparency in the process will help ensure that imports occur. Significant and growing quota quantities subject to tariffs that average between 1-3 percent.

- The right to import and distribute products without going through state-trading enterprise or middle-man.

- China has also agreed to the elimination of SPS barriers that are not based on scientific evidence and no export subsidies on agricultural products.

INDUSTRIAL PRODUCTS

China's commitments will eliminate broad systemic barriers to U.S. exports, such as limits on who can import goods and distribute them in China as well as barriers such as quotas and licenses that restrict imports of U.S. products.

TARIFFS

- Tariffs cut to an average of 9.4 percent overall and 7.1 percent on U.S. priority products.

- China will participate in the Information Technology Agreement (ITA) eliminating all tariffs on products such as computers, telecommunications equipment, semiconductors, computer equipment and other high technology products.

- In the auto sector, China will cut tariffs from the current 100% or 80% level to 25% by 2006, with the largest cuts in the first years after accession.

- Auto parts tariffs will be cut to an average of 10% by 2006.

- Significant cuts will also be made in the wood and paper sectors, going from present levels of 12-18% on wood and 15-25% on paper down to levels generally between 5 and 7.5%.

- China will also be implementing the vast majority of the chemical harmonization initiative. Under that initiative, tariffs will be at 0, 5.5 and 6.5 percent for products in each category.

ELIMINATION OF QUOTAS AND LICENSES

WTO rules bar quotas and other quantitative restrictions. China has agreed to eliminate these restrictions with phase-ins limited to five years.

- Quotas: China will eliminate existing quotas upon accession for the top U.S. priorities (e.g. optic fiber cable). It will phase-out remaining quotas, generally by 2002, but no later than 2005.

- Quotas will grow from current trade level at a 15% annual rate in order to ensure that market access increases progressively, and reduces the effect of quantitative restrictions.

- Auto quotas will be phased out by 2005. In the interim, the base level quota will be $6 billion (the level prior to China's industrial auto policy) and this will grow by 15% annually until

elimination.

RIGHT TO IMPORT AND DISTRIBUTE

Trading rights and distribution are the major priority of the manufacturing sector. At present, China severely restricts trading rights (the right to import and export) and distribution (wholesaling, retailing, maintenance and repair, transportation, etc.). Under the Agreement, China will provide, for the first time, trading rights and distribution rights to U.S. firms. Trading rights will be progressively phased in over three years. Distribution rights will be provided even for China's most restricted distribution sectors such as wholesale, transportation, maintenance and repair. China will provide for trading rights and distribution.

SERVICES

China has made commitments in all major service categories with reasonable transitions to eliminate most foreign equity restrictions (especially in sectors where the U.S. has a strong commercial interest), agreeing to accede to the Basic Telecommunications and Financial Services Agreements, and "grandfathering" of current market access for U.S. service providers.

GRANDFATHERING

China will grandfather all existing current market access and activities in all services sectors. This will protect existing American distribution services, financial services, professional and other service providers in China, including those operating under contractual or shareholder agreements or a license, from restrictions as Chinese commitments phase in.

DISTRIBUTION

In China today, foreign firms have no right to distribute products other than those they make in China, or to own or manage distribution networks, wholesaling outlets or warehouses. China also now frequently issues businesses licenses which limit the ability of American firms to conduct marketing, after-sales service, maintenance and repair and customer support. As the section on industrial goods noted, this is a severe barrier to goods exports as well as to service exports.

China's commitments address all these issues. They reflect a comprehensive commitment on distribution - including wholesaling, sales away from a fixed location, retailing, maintenance and repair, and transportation. Thus, Americans will be able to distribute imported products as well as those made in China, offering significant opportunity to expand U.S. exports of goods. As noted above, China will phase out all restrictions on distribution services for most products within three years.

SERVICES AUXILIARY TO DISTRIBUTION

Chinese commitments in services auxiliary to distribution include rental and leasing, air courier, freight forwarding, storage and warehousing, advertising, technical testing and analysis, and packaging services. All restrictions will be phased-out in 3 to 4 years, at which time U.S. service suppliers will be able to establish 100% wholly-owned subsidiaries.

TELECOMMUNICATIONS

China now severely restricts sales of telecommunications services and bars foreign investment. China's commitments mark its first agreement to open its telecommunications sector, both to the scope of services and to direct investment in telecommunications businesses. Through these commitments, China will become a member of the Basic Telecommunications Agreement.

Specific commitments include:

- Regulatory Principles: China has agreed to implement the pro-competitive regulatory principles embodied in the Basic Telecommunications Agreement (including cost-based pricing, interconnection rights and independent regulatory authority), and agreed to technology-neutral scheduling, which means foreign suppliers can use any technology they choose to provide telecommunications services.

- Scope of services: China will phase out all geographic restrictions for paging and value-added services in 2 years, mobile/cellular in 5 years and domestic wireline services in 6 years. China's key telecommunications services corridor in Beijing, Shanghai, and Guangzhou, which represents approximately 75% of all domestic traffic, will open immediately on accession in all telecommunications services.

- Investment: Under present circumstances, China allows no foreign investment in telecommunications services. With this agreement, China will allow 49% foreign investment in all services, and will allow 50% foreign ownership for value added paging services in two years, for mobile services, 49 percent in 5 years; and for inemational and domestic services, 49% in 6 years.

INSURANCE

For insurance, China now restricts foreign companies to operating in Shanghai and Guangzhou. Under the agreement:

- Geographic Limitations: China will permit foreign property and casualty firms to insure large-scale risks nationwide immediately upon accession, and will eliminate all geographic limitations IN 3 YEARS.

- Scope: China will expand the scope of activities for foreign insurers to include group, health and pension lines of insurance, which represent about 85% of total premiums, phased in over 5 years.

- Prudential Criteria: China agrees to award licenses solely on the basis of prudential criteria, with no economic needs test or quantitative limits on the number of licenses issued.

- Investment: China agreed to allow 50 percent ownership for life insurance. life insurers may now choose their own joint venture partners. for non-life, china will allow branching or 51% ownership on accession and form wholly owned subsidiaries in 2 years. reinsurance is completely open upon accession (100 percent, no restrictions).

BANKING

Currently foreign banks are not permitted to do local currency business with Chinese clients (a few can engage in local currency business with their foreign clients). China imposes severe geographic restrictions on the establishment of foreign banks.

- China has committed to full market access in five years for U.S. banks.

- Foreign banks will be able to conduct local currency business with Chinese enterprises starting 2 years after accession.

- Foreign banks will be able to conduct local currency business with Chinese individuals from 5 years after accession.

- Foreign banks will have the same rights (national treatment) as Chinese banks within designated geographic areas.

- Both geographic and customer restrictions will be removed in five years
- Non-bank financial companies can offer auto financing upon accession

SECURITIES

China will permit minority foreign owned joint ventures to engage in fund management on the same terms as Chinese firms. As the scope of business expands for Chinese firms, foreign joint venture securities companies will enjoy the same expansion in scope of business. Minority joint ventures will be allowed to underwrite domestic securities issues and underwrite and trade in foreign currency denominated securities (debt and equity).

PROFESSIONAL SERVICES

In the professional services, China currently tightly restricts operation of foreign law firms and accounting firms. In the Agreement, China has provided a broad range of commitments, including on legal, accountancy, taxation, management consultancy, architecture, engineering, urban planning, medical and dental, and computer and related services. China will permit foreign majority control except for practicing Chinese law (an exception common to many WTO members.) For accountancy, China has agreed to eliminate a mandatory localization requirement and will now allow unrestricted access to its market to professionals licensed and follow transparent procedures.

AUDIOVISUAL

China's commitments cover the right to distribute video and sound recordings and cinema ownership and operation. For video and sound recordings, China will allow 49% foreign participation in joint ventures engaged in the distribution of these products. China has also agreed to import 40 films after accession growing to 50 films in three years, of which 20 films will be revenue sharing in each of the three years.

TRAVEL AND TOURISM

Hotels: China will allow unrestricted access to the Chinese market for hotel operators with the ability to set up 100% foreign owned hotels in 3 years, with majority ownership allowed upon accession.

Travel Services: Foreign travel operators can provide the full range of travel agency services. For travel agency services, China will allow access to government resorts as well as Beijing, Shanghai, Guangzhou and Xian.

PROTOCOL PROVISIONS

Commitments in China's WTO Protocol and Working Party Report establish rights and obligations enforceable through WTO dispute settlement procedures. We have agreed on key provisions relating to antidumping and subsidies, protection against import surges, technology transfer requirements and offsets as well as practices of state-owned and state-invested enterprises. These rules are of special importance to U.S. workers and business.

China had agreed to implement the TRIMs Agreement upon accession, eliminate and cease enforcing trade and foreign exchange balancing requirements, eliminate and cease enforcing local content requirements, refuse to enforce contracts imposing these requirements; and only impose or enforce laws or other provisions relating to the transfer of technology or other know-how, if they are in accordance with the WTO agreements on protection of intellectual property rights and trade-related investment measures.

These provisions will also help protect American firms against forced technology transfers, as China has also agreed that, upon accession, it will not condition investment approvals, import licenses, or

any other import approval process on performance requirements of any kind, including: local content requirements, offsets, transfer of technology, or requirements to conduct research and development in China.

ANTIDUMPING AND SUBSIDIES METHODOLOGY

The agreed protocol provisions ensure that American firms and workers will have strong protection against unfair trade practices including dumping and subsidies. The U.S. and China have agreed that we will be able to maintain our current antidumping methodology (treating China as a non-market economy) in future anti-dumping cases. this provision will remain in force for 15 years after china's accession to the WTO. Moreover, when we apply our countervailing duty law to China we will be able to take the special characteristics of China's economy into account when we identify and measure any subsidy benefit that may exist.

PRODUCT SPECIFIC SAFEGUARD

The agreed provisions for the protocol package also ensure that American domestic firms AND WORKERS will have strong protection against rapid increases of imports.

To do this, the Product-Specific Safeguard provision sets up a special mechanism to address increased imports that cause or threaten to cause market disruption to a U.S. industry. China is a major exporting country that enjoys open access to U.S. markets. This mechanism, which is in addition to other WTO Safeguards provisions, differs from traditional safeguards measures. It permits United States to address imports solely from China , rather than from the whole world, that are a significant cause of material injury through measures such as import restrictions. Moreover, the United States will be able to apply restraints unilaterally based on legal standards that differ from those in the WTO Safeguards Agreement and could permit action in more cases. This provision will remain in force for 12 years after China accedes to the WTO.

STATE-OWNED AND STATE-INVESTED ENTERPRISES

The Protocol addresses important issues related to the Chinese government's involvement in the economy. China has agreed that it will ensure that state-owned and state-invested enterprises will make purchases and sales based solely on commercial considerations, such as price, quality, availability and marketability, provide U.S. firms with the opportunity to compete for sales and purchases on non-discriminatory terms and conditions.

China has also agreed that it will not influence these commercial decisions (either directly or indirectly) except in a WTO consistent manner. With respect to applying WTO rules to state-owned and state-invested enterprises, we have clarified in several ways that these firms are subject to WTO disciplines.

-Purchases of goods or services by these state-owned and state-invested enterprises do not constitute "government procurement" and thus are subject to WTO rules.

-We have clarified the status of state-owned and state-invested enterprises under the WTO Agreement on Subsidies and Countervailing Measures. This will help ensure that we can effectively apply our trade law to these enterprises when it is appropriate to do so.

TEXTILES

China's protocol package will include a provision drawn from our 1997 bilateral textiles agreement, which permits U.S. companies and workers to respond to increased imports of textile and apparel products. This textile safeguard will be in effect until December 31, 2008 which is after the WTO Agreement on Textiles and Clothing expires.

EXHIBIT 2

Inside US Trade

U.S.-CHINA WTO DEAL ALLOWS CURBS ON EXPORTS FOR 12 YEARS

Date: November 16, 1999

The bilateral U.S.-China market access deal struck over the weekend to pave the way for China's entry into the World Trade Organization contains safeguard provisions that would allow the United States to keep Chinese products out of its market until twelve years after accession. This product-specific safeguard would allow the U.S. to curb imports from China that "cause or threaten to cause market disruption" to a U.S. industry, according to a Nov. 15 fact sheet issued by the Clinton Administration.

This is a lower standard than the WTO Safeguard Agreement, which can only be invoked for global imports, not for products from a specific country, the fact sheet said.

But under this product-specific safeguard, China could also protect its market against U.S. exports by setting quotas, according to the fact sheet.

The safeguard "permits China to address imports that are a significant cause of material injury through measures such as voluntary restraints," the fact sheet said. USTR officials could not be reached to verify this information.

The standard in the WTO Safeguards Agreement allows countries to impose safeguards against imports that cause or threaten to cause "serious injury" to a domestic industry. In the spring, when the U.S. and China came close to a bilateral WTO deal, the Administration defended the market-disruption standard as being consistent with Section 406 of the 1974 Trade Act.

To fight unfairly priced Chinese exports, the bilateral deal allows the use of non-market economy (NME) methodology in antidumping cases for 15 years, U.S. Trade Representative Charlene Barshefsky announced in a Nov. 15 press conference in Beijing. China had initially insisted on a five-year phaseout for NME methodology, which tends to produce higher dumping margins than the methodology applied to market economies.

In contrast, the U.S. had insisted there could be no phaseout of the NME methodology and that China had to prove within the context of individual dumping cases that a certain production sector is driven by market factors. This provision is of major importance to the semiconductor industry as well as the U.S. steel and textile industries.

The Administration fact sheet implies that the U.S. may change its current practice of not applying countervailing duty law to China as a non-market economy, but does not explicitly state this is the case. As a result of a mid-1980s court decision, the U.S. as a matter of practice, not statute, upholds that there can be no subsidies cases against an NME, industry sources said. This is based on the notion that it is impossible to assess the distortion in a market from subsidies if there is no free market, they said.

The fact sheet only addresses the subsidies issue in one sentence. "[W]hen we apply our countervailing duty law to China, we will be able to take the special characteristics of China's economy into account when we identify and measure any subsidy benefit that may exist," the fact sheet said.

Commerce Dept. officials could not clarify this provision at press time.

The bilateral WTO agreement also includes a specific safeguard to protect the U.S. textile market until Dec. 31, 2008, or four years after quotas expire on China's exports to the U.S., Barshefsky said in the Nov. 15 Beijing news conference. The textile provisions reflect the terms of a WTO agreement struck by then USTR Chief Textile Negotiator Rita Hayes in 1997, which means the U.S. backed off its demands for an extension of quotas for five years, according to Barshefsky.

The new agreement constitutes the "incorporation in full of our bilateral textiles agreement," she said.

That agreement, which was negotiated when the U.S. and China struck a deal governing access to the U.S. market, foresees a quota phaseout by 2005 and a four-year safeguard to be invoked under the market disruption standard contained in the Multifiber Arrangement (*Inside U.S. Trade*, Feb. 7, 1997, p. 7). Because of industry opposition, the Administration then sought to extend the phaseout for another five years.

However, it is uncertain whether the U.S. and China changed the standards under which the textile safeguard could be invoked from the market disruption standard agreed in 1997. Before the U.S. delegation left for China, there was some interagency discussion of whether to make it harder to invoke the textile safeguard, according to informed sources.

Business sources said this week that the U.S. "flexibility" on textiles led to additional Chinese concessions on investment, which helped cinch the agreement on Nov. 14. The final agreement allows investment in the internet as well as the telecommunications sector at a level lower than announced in April, according to Barshefsky.

In telecommunications, China will initially allow 49 percent ownership, moving to 50 percent two years after accession, according to the fact sheet. But it does not specify whether China insisted that an individual company's share in a joint venture be limited to 10 percent (*Inside U.S. Trade,* May 14, p.10).

Barshefsky, USTR General Counsel Bob Novick, and Gene Sperling, the President's Economic Advisor, are slated to return to Washington late today (Nov. 16). Both Senate Finance Committee Chairman Bill Roth (R-DE) and House Ways & Means Committee Chairman Bill Archer (R-TX) are planning to hold hearings as early as this week to get a first hand account of the agreement from Barshefsky, congressional sources said.

But the Administration expects to submit its request for permanent most-favored nation status for China to Congress "sometime early next year," according National Security Advisor Samuel Berger, who spoke in Turkey on Nov 15. He expressed the hope that the request would garner broad support.

In a related development, key Republican and Democratic lawmakers yesterday said they would withhold judgment on the agreement until they have had a chance to be briefed on the details.

The U.S. delegation led by Barshefsky left for China on Nov. 8. The delegation did not include USTR Chief Textile Negotiator Don Johnson, Special Agriculture Negotiator Peter Scher or officials from the Agriculture Dept. U.S. officials insisted that they were not needed because the agriculture agreement would not be reopened.

Agriculture industry sources said yesterday that they believed China had not clawed back any concessions from the deal negotiated in the spring, but admitted they had no first-hand information.

This absence of exact detailed information also prevented industry groups from offering specific

endorsement of the agreement.

The Administration initially distributed a transcript of the Barshefsky press conference, and then the fact sheet later in the day.

Both Barshefsky and the fact sheet failed to explicitly compare the final deal to the one outlined by USTR in April 8 summary of alleged Chinese commitments, and some business representatives also tried to distance themselves from earlier remarks that a final deal had to reflect the April 8 outline released by USTR. Labor groups expressed their opposition to the deal (see related story).

But it is apparent from comparing the Nov. 15 and April 8 documents that China backtracked on auto tariffs, which would be cut to 25 percent by 2006 instead of 2005 as announced in April. But one source held out the possibility that the phaseout of the auto tariffs would be more frontloaded than had initially been proposed. The Administration announced that these tariff cuts would be made in equal installments.

Similarly, comparison of the documents shows that China backtracked on the investment levels on insurance and telecommunications.

The transcript of Barshefsky's remarks and the fact sheet also offer conflicting information about the tariff cuts contained in the final agreement. In the press conference, she announced that China's industrial tariffs "on the average would decline to about seventeen percent," but the fact sheet says that industrial tariffs will fall to an overall average of 9.4 percent by 2005. That is nominally the same as the April deal unilaterally announced by the U.S., but constitutes longer phaseout for many of them.

In April, USTR announced that "two-thirds of tariff cuts will be implemented by 2003," with the balance phased in by 2005 with some exceptions (*Inside U.S. Trade,* April 9, p. 1).

Similarly, informed sources said that the provisions on forced technology transfer and the operation of state-trading enterprises based on commercial principles were changed from April. But the Administration insists that these are only minor changes to these provisions that would not weaken the substance of the agreement.

Regardless of the actual wording, some sources have questioned whether any agreement on forced technology transfer could be enforced. The Nov. 15 fact sheet only says that the final agreement includes protection against technology transfer requirements and offsets as well as practices of state-owned and state-invested enterprises.

"These provisions will also help protect American firms against forced technology transfer, as China has also agreed that, upon accession, it will condition investment approvals, import licenses, or any other import approval process on performance requirements of any kind: local content requirements, offsets, transfer of technology, or requirements to conduct research and development in China," the fact sheet said.

Once other trading partners have struck a bilateral deal with China on its WTO entry, WTO members must work out final details on the draft protocol and write the working party report, officials said this week. For example, the provisions on sanitary and phytosanitary measures as well as the protocol annex on non-tariff barriers need further work, one source said.

If drafting begins soon, these issues may be able to be settled in one working party meeting early next year, officials said. The full package would then have to be vetted in capitals of various trading partners

before being finally approved by the WTO General Council, they said. The time period between the working party conclusion and the General Council vote may take about three to four weeks, according to these officials.

Once approved by the WTO, China's entry into the WTO would go into effect once China ratifies it, they said.

The European Union expects to meet with China on its bilateral agreement as early as this week, and Canadian officials held a bilateral meeting with China before the U.S. delegation did, but did not yet deal with financial and telecommunications services, informed sources said.

Key members of Congress on both sides of the aisle yesterday took a wait-and-see attitude. Senate Majority Leader Trent Lott (R-MS) said in a Nov. 15 statement that he would "reserve judgment" until he can examine the details of the agreement. "While China's admission to the WTO could provide opportunities for U.S. businesses, there remain significant questions about whether an agreement with China can be enforced fully and fairly, and about the effect that it could have on religious freedoms, human rights, and our national security," Lott said in the statement.

Democratic members of the House voiced a similar message. House Democratic Leader Richard Gephardt (D-MO) will assess the agreement on its merits along with its enforcement provisions, sources said. In addition, he will insist that China take other non-trade measures in such areas as human rights, they said.

In a separate statement, Rep. Nancy Pelosi (D-CA) also highlighted "the crucial issues of implementation and enforcement" if a deal is to be acceptable to Congress. Rep. Sander Levin (D-MI) also said the agreement requires a careful examination of the market access and safeguards provisions, according to a Nov. 15 statement.

Copies of the transcript of Barshefsky's Nov. 15 press conference as released by USTR, a Nov. 15 USTR press release on the U.S.-China agreement, along with an article by the official China news agency Xinhua released by the Chinese embassy are available on Inside U.S. Trade's website World Trade Online, along with numerous reaction statements from labor and industry groups. Call for access to the site.