WRITTEN TESTIMONY OF DEPUTY U.S. TRADE REPRESENTATIVE KARAN K. BHATIA
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U.S.-China Trade Relationship

Introduction

Chairman Levin, Ranking Member Herger and distinguished members of the Ways and Means Subcommittee on Trade, I am delighted to be able to participate in the first of what I understand is to be a series of hearings on U.S.-China trade relations. As the Deputy U.S. Trade Representative with principal responsibility for our Asian and African trade relationships, I can tell you that there are few subjects that I deal with that are more important or more complex than our relationship with China, and I'm very pleased that this subcommittee is devoting time to this subject.

I understand that today's hearing is focused principally on two topics: (i) subsidies and (ii) the enforcement of intellectual property rights. I will touch on both subjects. But, especially because this is the first of a number of hearings that the Subcommittee intends to conduct, I thought it might be helpful to provide a brief overview of the U.S.-China trade relationship generally and developments in that relationship over the past 12 months.

Top-to-Bottom Review

One year ago yesterday, USTR issued a comprehensive, interagency "Top-to-Bottom Review" ("T2B" or "Review") of U.S.-China trade relations. That Review observed the policy of economic engagement the U.S. has pursued with China for the past 25 years – on a largely bipartisan basis across administrations – has benefited both countries. The Review also noted that, after a period in which U.S. trade policy was largely focused on bringing China into the international trading system and urging China to implement its new WTO commitments during a transition period, the relationship is now entering an important new phase – one in which China will be held fully accountable for its WTO obligations as a mature trading partner and will be expected to play a greater role in strengthening the global trading system commensurate with its economic heft and the economic benefits it receives. The Review urged, as we enter this new period, the readjustment of U.S. trade resources and priorities with respect to China – in favor of enhanced use of enforcement tools and more focused, coordinated and senior-level dialogue.

The T2B set forth a number of key objectives: (i) strengthening the focus on China's WTO compliance and adherence to international norms, (ii) ensuring that the bilateral trade relationship offers more balanced opportunities and is equitable and durable, (iii) making U.S. trade policymaking more proactive and informed by more comprehensive information and more coordination, (iv) encouraging China to participate more fully in the global trading system, and (v) ensuring that the United States remains an active and influential economic and trading power in the Asia Pacific region. The T2B also set forth a detailed list of steps to achieve those objectives.

Top-to-Bottom Review – Implementation

Looking back over the past year, I am pleased to report that, after the opportunity to consult with Congress, we have moved full-steam ahead to implement the recommendations laid out in the T2B. Let me run through a few:

- We demonstrated our willingness to use WTO dispute settlement to hold China to its commitments. Under Ambassadors Portman and Schwab, we filed WTO cases on China's discriminatory treatment of imported auto parts and use of prohibited subsidies. And we were on the verge of filing a third case last year, challenging China's antidumping order against U.S. exports of Kraft Linerboard, when China rescinded that order just hours before our filing.

- In April 2006, we held a meeting of the Joint Commission on Commerce and Trade (JCCT). At that meeting, we obtained Chinese commitments to address a number of concerns about access to China's market, transparency, and enforcement of intellectual property rights. President Bush also had an opportunity to discuss important economic issues with President Hu Jintao during his visit to the United States.

- In September, President Bush launched a new high-level dialogue to address critical economic issues – the Strategic Economic Dialogue (SED). The first SED meeting was held in Beijing in December, and we have been pushing forward with a number of specific follow-up discussions in anticipation of the next SED meeting here in May. To further bolster the initiative, Secretary Paulson recently announced that Treasury has appointed Ambassador Alan Holmer as Special Envoy to China overseeing the SED process.

- We have launched a new and unprecedented provincial level review of China's IPR enforcement efforts, and look forward to publishing the results later this Spring.

- We have held dozens of sector- or issue-specific negotiations with the Chinese in areas ranging from beef to telecommunications, as we seek to ensure that China continues to open its markets and honor its commitments.

- We have held 61 meetings or briefings with Congress over the past year regarding our China trade relationship and have regularly consulted on such topics as our WTO litigation strategy, the JCCT dialogue, and the SED.

- We have created a senior-level China Task Force within our Advisory Committee on Trade Policy and Negotiations.

- We have established new channels of communication with our third country trading partners to coordinate trade policy with respect to China.

- And at USTR, over the past year, we have substantially strengthened our China-focused resources, with the creation of the position of Chief Counsel for China Trade Enforcement, the creation of a China Enforcement Task Force, the addition of new staff in our China Office, and the hiring of a new USTR attaché in Beijing.

These and the many other actions we have taken to implement the T2B strategy over the past year have been important, both individually and collectively. They demonstrate to U.S. stakeholders, to China, and to our other trading partners that we have a carefully crafted strategy for engaging China on trade matters, and that we have been following it.

Of course, both the T2B and the actions taken to implement it are means to an end, not an end in itself. The end is a trade relationship with China that is more balanced in the opportunities it offers, more equitable and more durable. Such a relationship will not be achieved within the span of a mere 12 months. But I am pleased to say that there are some encouraging signs. Let me point to three:

- Based on the results just reported by the Commerce Department, U.S. exports to China last year climbed by 32 percent. (By contrast, I would note that China's exports to the U.S. increased by 18 percent.) This suggests that the Chinese market is becoming more accessible for American companies, and that Chinese consumers are developing an appetite for America's highly competitive goods and services. China today has become our fourth largest export market, and the fastest growing major export market for the United States in the world. It is helping to support thousands of American jobs today and will support even more in the future.

- In its 2006 annual survey of members, the U.S.-China Business Council reported that 81 percent of members surveyed reported that their Chinese operations are profitable (with more than half saying that profitability rates for their China operations meet or exceed global profit margins) and 97 percent of respondents saying that they are optimistic about prospects for their China business over the next five years.

- There have been a number of important transactions that have helped to further open the Chinese market to U.S. companies – including the acquisition of a stake in Guangdong Development Bank by Citibank, the selection of Westinghouse for a $5-8 billion nuclear power contract, and the signing of over 100 purchase agreements and contracts worth over $16 billion in advance of President Hu Jintao's visit to the United States last April.

In citing these positive developments, I do not mean to suggest that all is well in the U.S.-China economic relationship. Significant challenges remain. In particular, as detailed in the 2006 Report to Congress on China's WTO compliance that USTR issued last December, we are concerned by signs that China could seek to slow down or pull back from the market-oriented and WTO-consistent changes they have been making in their economy and pursue more state interventionist or mercantilist policies. A retreat from continued reform would slow China's own economic development, dampen U.S export growth, preclude the leveling of imbalances, and breed frustrations. So, working to ensure that China does not slow down or retreat from reform is a key objective.

Let me now turn to the two specific topics at issue here today – subsidies and IPR – and briefly discuss the most recent developments in our dealings with the China on these two topics.

Subsidies

In testimony last year before the Senate Finance Committee, I observed that the Chinese Government's role in directing the Chinese economy, including through the use of subsidies, was one of the principal concerns of USTR. The way we have approached this issue over the past twelve months is entirely consistent with the strategy laid out in the T2B – we are confronting this serious challenge using both enforcement levers as well as dialogue.

As you know, just two weeks ago we announced that the United States has requested consultations at the WTO over what we contend is China's persistent use of prohibited subsidies. Basically, the United States believes that China uses its tax laws and other tools to encourage exports and to discriminate against imports of a variety of manufactured goods. The subsidies at issue in this case are offered across a broad array of industry sectors in China -- including steel, wood products, information technology, and others.

It is an important case – important because it challenges policies that are tilting the playing field against our workers and companies, important because it makes clear that we will use WTO dispute settlement procedures to hold China to its commitments where dialogue does not resolve our concerns, and – perhaps most of all – important because it will help impel China to maintain a process of reform and to redirect its economy towards a model of consumption-led, rather than export-led, growth.

While we have filed this WTO case, we continue to engage in dialogue with the Chinese on their use of subsidies. These discussions are happening both at the sector-specific level – for example, our recently created "Steel Dialogue" under the JCCT is enabling a conversation among governments and industries of both sides – as well as in connection with our broader economic dialogues, including the Strategic Economic Dialogue. Industrial policies that limit market access for non-Chinese origin goods and that provide substantial government resources to support Chinese industries also remain a concern.

Finally, although it does not fall within USTR's statutory purview, I should note that the Department of Commerce continues to apply U.S. trade remedy laws to ensure that unfair trade practices, whether undertaken by the Chinese or others, do not distort the playing field against U.S. companies.

IPR Enforcement

The Administration is similarly employing a dual-track approach in the area of intellectual property rights. The rampant infringement of intellectual property rights that persists in China, in spite of efforts by central government officials to move against illegal practices, not only robs U.S. businesses of billions of dollars a year in legitimate sales, it also weakens China's development of its own knowledge-based industries.

Over the past year, we have been working to prepare a WTO case that challenges China's compliance with its WTO obligations in the area of intellectual property rights enforcement. Last October, we informed China that we would be filing such a case, but then agreed to hold off, with the support of U.S. industry, when China asked for further bilateral discussion. We have been holding those discussions, including late last month in Beijing. We have also been raising with China restrictions on market access. While these are not IPR issues per se, they have a negative impact on the industries depending on intellectual property, such as the copyright industry and, to a certain extent, they exacerbate some of the problems with IPR enforcement. Thus far, no settlement has been reached. We are consulting with Congress and with industry on next steps. If we believe that negotiations offer a reasonable chance of success, we will continue to pursue them – a successfully negotiated outcome can be more efficient and as successful as a litigated outcome. But if it becomes clear that negotiations will not be successful, then we will proceed with WTO dispute settlement.

In the interim, of course, we continue to try to work with China through various other avenues to address this serious problem. For example, under Special 301, we are conducting a special review of enforcement at the provincial and municipal levels of government where much of the responsibility for day-to-day enforcement lies. We are also continuing to press China to make improvements in its IP system through the JCCT and SED.

It bears noting that at the highest levels of the Chinese government there is a clearly stated commitment to tackle this problem. In his remarks from the South Lawn of the White House in April, President Hu affirmed that China is committed to "strengthening the protection of intellectual property rights.**”** China’s leadership appears to recognize that the development of a more vigorous and effective IPR enforcement system is critical not only to trade relations with the United States, but also to China’s own economic development. The challenge confronting China is turning those stated commitments into real results.

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Thank you for the opportunity to testify. I will be happy to take your questions.