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**U.S. China Commission February 3, 2005 Public Hearing on
China's Compliance with its WTO Commitments**

Introduction

Mr. Chairman, members of the Commission, thank you for the opportunity to testify today on behalf of the State Department to discuss our assessment of China's compliance with its World Trade Organization (WTO) commitments.

On December 11, 2004, China marked the 3rd year of its accession to the WTO. This milestone marked China's continued commitment to ongoing tariff liberalization, as well as new, important steps in the areas of trading and distribution rights and investment. I'd like to begin with the State Department's overall assessment of China's WTO compliance, and then mention some specific areas of concern. I would also like to highlight the State Department's special role with regard to working with China on its WTO commitments. I look forward to responding to your questions related to our approach to China's WTO implementation.

Overall Assessment of China's Compliance with its WTO Commitments

Overall, since December 2001, there is much to be pleased with, and, in general, China's leadership has made an effort to bring China into formal compliance with its WTO commitments. China's efforts include extensive tariff reductions, regulatory reform and harmonization, and significant legal changes. China deserves due recognition for this concerted effort.

This general assessment notwithstanding, it must be acknowledged that China's compliance record has been uneven over the past three years. 2003, in particular, was a year in which we and American businesses in China became concerned with both the slowdown in the pace of implementation and the significant WTO-related problems as new regulations and laws were promulgated and implemented. From problematic IPR enforcement and industrial policies such as the discriminatory use of value-added taxes to problems with agriculture (non-transparent and scientifically questionable

application of SPS measures) and services (excessive capital requirements in many sectors), we at State, as well as all the agencies tasked with monitoring China's WTO compliance, were engaged fully to address these issues. Fortunately, with determined, coordinated efforts, we and our interagency colleagues were able to substantially improve the situation. We were able to resolve a number of outstanding issues in 2004, using the highly effective mechanism of the elevated Joint Commission on Commerce and Trade (JCCT). When discussions and negotiations did not work, we did not hesitate to use legal recourse available to us, such as our successful use of the WTO dispute resolution mechanism in the semiconductor VAT case.

U.S. stakeholders were significantly more satisfied with China's WTO performance in 2004 than in previous years. Nevertheless, serious problems remain, and new problems regularly emerge. Many of the concerns from 2003 have now been settled and cleared. U.S. exports to China continued to increase dramatically in 2004, as they have done every year since China joined the WTO, reaching \$34bn. China is now our 5th largest export market, up from 11th place in 2001, and exports are up 80% since China's WTO entry.

Key Areas of Concern

Although China's performance in 2004 showed marked improvement over its performance in 2003, there remains a substantial agenda of trade issues. Most notably, inadequate protection of intellectual property rights (IPR) remains our most serious bilateral economic concern.

The good news is that China has made strides in bringing its legal system into compliance with the WTO's Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS Agreement). Specifically, it has created a multi-agency IP task force headed by Vice Premier Wu Yi, and its top court has recently promulgated a new "judicial interpretation" allowing greater use of criminal statutes (vice administrative) against IP violators. Raids against infringing markets and production facilities have netted tens of millions of infringing copies. However, the bad news is that neither we, nor the Japanese and Europeans, have not seen a corresponding reduction in piracy and counterfeiting rates, and the reality on the ground remains that IP problems in China are pervasive, both at the small-scale and commercial-scale ends of the spectrum, in copyright, trademark and patent infringement. Simply put, we must see substantial improvement in 2005, and the State

Department will work with the new IP Negotiator as well as the IP Policy Coordinator, both created by Congress in 2005 budget legislation, to ensure that China makes progress on this vital front. Secretary Rice promised the Senate that she would pay close attention to the IP problem in China.

Apart from the IP situation, we remain concerned about China's WTO compliance in specific industry sectors as well as in the critical arena of transparency. For example, we see problems with customs valuation on certain products as well as with proposed direct selling regulations and proposed legal changes governing the provision of express delivery services. China agreed to liberalize distribution rights on as December 11, 2004; but has yet to issue guidance to clarify for firms and officials how to implement these liberalizations. This is of serious concern — the right to freely distribute goods within the whole Chinese market as well as the right to provide logistics and other high-value added services to Chinese industrial and retail chain customers is at the heart of the next phase of China's integration into the global market.

We are also troubled with issues that are not easily defined as WTO-accession problems, but that are serious all the same, such as the growing issues of standards as technical barriers to trade. We have seen a disturbing trend of China using high technology standards-setting in order to benefit its domestic industry, a tactic that undermines the general practice of industry reliance on international standards-setting bodies that create harmony and a sturdy playing-field for everyone. We will continue to work with China to underscore the benefits to industries and consumers to use global standards-setting mechanisms. Similarly, we are carefully watching the issue of government procurement of software, an issue that has come to the fore in recent months. We are working with the Chinese government and U.S. industry to ensure access to government purchasers, one of the few licit markets for legitimate software in China. We also actively encourage China to join the WTO Government Procurement Agreement as soon as possible, fulfilling China's WTO promise to begin the process to join the group.

We also remain troubled by the lack of transparency in Chinese regulation drafting processes, particularly those conducted by non-MOFCOM bodies. The Administration will continue to strictly enforce its trade laws to ensure that U.S. interests are not harmed by unfair trade practices.

U.S. Government Approach, and the State Department Approach for Achieving Broader and Better Compliance from China

Since mid-2003, the Administration's strategy to engage China on economic matters has been to interact with Chinese officials both multilaterally and bilaterally at senior and working levels. We interact regularly on a broad range of issues, underscoring the essential nature of making tangible progress for the American people.

Administration officials, from the Deputy Assistant Secretary level up to the Cabinet level, dedicate significant amounts of time to our efforts. Officials, such as Mr. Levine and his counterparts in USTR, USDA and other agencies log significant miles traveling to Beijing and hosting their counterparts here. Deputies Shiner and Aldonas do much the same, often in advance for meetings with their Principals. Secretary Evans recently traveled to China. The effort is time-consuming, but pays off. Significant issues are frequently resolved bilaterally, due to the intense, high-level groundwork being laid nearly continuously. The "WAPI" wireless computing standard issue, which generated focused interest by some of our most competitive high tech firms, is an excellent case in point: intensive interaction over many months finally produced a resolution acceptable to both parties, a resolution that would in all likelihood have been impossible without that level of engagement. Multilaterally, this Administration devotes equal attention and effort, using the WTO Transitional Review Mechanism vigorously to make key points with the Chinese, often joining our efforts with other countries with similar concerns.

The Department of State has a unique role in this process and the Administration's overall strategy. State not only facilitates ongoing engagement with the Chinese and all of the USG's front line economic agencies, but is an equal player among Agencies in Washington when it is time to make decisions. Our officials based at the Embassy in Beijing and our four Consulates General work with their colleagues in the other USG agencies every day, analyzing how Chinese thinking is evolving vis-à-vis these ongoing issues and explaining U.S. positions to tough Chinese officials. I personally participate in JCCT Working Groups and meet with visiting Chinese officials. Our Assistant Secretary recently sponsored a conference in Hong Kong for all of our mission personnel posted in East and South Asia and the Pacific who deal with IP issues. Our Under Secretary Larson chairs the State Department's dialogue with the State Council's

influential National Development and Reform Commission, a dialogue focusing on long range macroeconomic restructuring issues such as the development of agribusiness, adoption of clean energy solutions, SOE restructuring, and how to integrate advanced M&A techniques into economic reform strategies. Our U/S along with our Secretary and Deputy Secretary regularly participate in WH meetings in which China economic strategy is decided. In addition to the considerable staff dedicated to WTO compliance at our Embassy in Beijing, State also has a number of officers in Washington focusing on these issues, both in our East Asia and Pacific Bureau and our Economic Bureau. Most are experienced mid and senior-level officers with extensive policy experience in Washington and overseas.

Conclusions

US-China economic and commercial relations portfolio are central to our overall relationship, and to US interests. Nowhere are the stakes for our economy and American workers higher. I remain confident that China's leadership is dedicated to fulfilling its WTO obligations, despite inevitable problems that occur. And where problems occur, specifically on lax IPR enforcement, this Administration will push China to live up to its WTO commitments. The State Department will continue to play a significant role in this process to ensure that our engagement with China continues to pay dividends for our companies, workers and economy.