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Before the U.S.-China Economic and Security Review Commission

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China and the WTO: Assessing and Enforcing Compliance
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On behalf of the member companies of the United States Association of Importers of Textiles and Apparel, we are pleased to respond to the Commission's request to participate in the hearing, "China and the WTO: Assessing and Enforcing Compliance." The Commission has requested comments from the textile and apparel community with respect to "strategies for enforcing China's textile commitments" under its World Trade Organization Accession Agreement. In addition, the Commission provided a list of specific questions to which we will respond in this statement.

Before beginning a response to those questions, we do want to start with our recognition that the essential mandate for the Commission is to review compliance by China with the WTO Accession Protocol and also to "explore what incentives and policy initiatives should be pursued to promote further compliance by China." We believe that the textile and apparel sector plays a critical role in the exploration of incentives and the impact of U.S. policy initiatives on compliance activities by China. The landscape of the broad economic and political relationship between the United States and China has changed now that we are in 2005. And while we did not volunteer for the role, the textile and apparel sector is at the center of decisions that will affect the U.S.-China relationship for years.

For more than 40 years, the international quota system significantly distorted all segments of the international textile and apparel trade. On January 1, 2005, the quota system ended for all countries that are members of the World Trade Organization. The elimination of the discriminatory quota system – which restricted investment in the developing countries – was hailed as a major success of the Uruguay Round Agreement. And it certainly reflected one of the few times that the international community negotiated a smooth conclusion to a protectionist system. The elimination of the quotas was phased out over ten years – a lengthy phase-out but one that allowed all companies and countries to plan for the changes in the industry. As the WTO Director General stated at the final meeting of the Textiles Monitoring Body:

> *The expiry of the ten-year transition period of ATC implementation will put an end to a special and discriminatory regime that has lasted for more than 40 years. With the full and timely implementation of the ATC, trade in textile and clothing products will cease to be subject to this regime and become governed by the general rules and disciplines embodied in the multilateral trading system. Hence the completion of the*

integration process under the ATC will not only contribute to increasing trading opportunities, but will also be of major systemic importance.

...

All in all, the elimination of the trade-distorting quantitative restrictions that are still in place will be beneficial for the global economy in terms of increased market access opportunities, efficiency gains and consumer welfare.

While China joined the WTO only in 2001, the elimination of the quota system was one of the positive developments for the Chinese economy. The ability to rationalize the textile and apparel factories, and to eliminate those suppliers who were propped up only because they were guaranteed an allocation of the scarce quotas, is believed to be an important step in the move in China from a state-controlled economy to a market economy. That opportunity for China to expand production of textile and apparel products also offers an important avenue for incentives that the United States can use to ensure compliance with other WTO commitments by China. There is a clear linkage between the U.S. elimination of the quota system and the early implementation of other WTO commitments by China.

Even though today China is the number one supplier for textile and apparel imports to the United States, the fact is that when we review the U.S. import statistics for the apparel products with the highest consumer demand, the quota system has meant that China is a relatively minor supplier of those products. For example, if we review the U.S. imports of cotton trousers and shorts, China ranks as twenty-third largest supplier. China sells fewer pairs of cotton pants to the U.S. market than Jordan, Lesotho, or even Russia, which is not even a WTO member country. We realize that some speakers may say that this merely highlights the "threat" from China. But we think that it should be recognized by the Commission as an opportunity. There is no question that in a rational economic world that is not distorted by the quota system, China will gain market share. And the commitment by the United States to allow growth in the imports from China – which will certainly come at the expense of shifts from other, less efficient suppliers – will provide strong support to the credibility of U.S. trade officials when they press for more market opening in the Chinese economy for U.S. manufacturing exports.

Let us now turn to the responses by USA-ITA to the questions that were specifically asked by the Commission. First, the Commission asks about the impact of the termination of the Multi-Fiber Arrangement on the U.S. textile and apparel industries. Our member companies see a positive long-term impact for the sector. The elimination of the global bureaucracy that was needed to administer the complicated quota system should mean that resources will no longer be diverted from commercial activities. Over time this should mean positive cost savings for U.S. companies and for U.S. consumers.

Second, the Commission asks whether the textile safeguard mechanism included as part of China's accession to the WTO "is an effective mechanism for dealing with post-MFA surges." Certainly China made a substantial concession by agreeing to remain the *only* WTO member country that will continue to be subject to a separate safeguard process against textile and apparel imports. USA-ITA believes that the Textile Safeguard is an effective way to deal with post-MFA surges from China. Even the existence of the Textile Safeguard mechanism through 2008 serves as a deterrent to U.S. companies that might otherwise place new orders in China.

Companies make sourcing decisions based on a variety of factors – but one of those factors is a desire for predictability and certainty. The China Textile Safeguard introduces four years of uncertainty – even if the United States never uses the safeguard.

However, in many ways, we would suggest that the wrong question is being asked. While today's hearing is about U.S. relations with China, the fact is that the quota system was eliminated on all WTO member countries, which includes a number of other major suppliers to the U.S. market. In the context of the quota elimination, we suggest that the question could be revised to ask what steps industries took during the term of the MFA and its successor, the Agreement on Textiles and Clothing, to prepare for increased competition from imports (from all sources) in the absence of protection, and whether the United States has taken the most effective steps to promote production in this hemisphere. The answer to both questions is no. Some manufacturers have implemented strategies to compete globally and are certainly going to benefit from that foresight. Many others, however, have not, perhaps in part because they did not believe that the protection would ever end. The United States also has established preference arrangements and negotiated free trade agreements that include textile and apparel products. But the restrictive rules established under those arrangements are not as attractive as they could be, if we want to truly encourage partnerships in this hemisphere and enhance the competitiveness of both U.S. and other Western Hemisphere manufacturers. USA-ITA strongly supports quick approval for the Central American Free Trade Agreement (CAFTA). The best mechanism to maintain yarn and fabric production in the United States is to enhance the competitiveness of the Central American apparel industry. The partnership that exists – particularly with duty-free treatment for all apparel made in Central America and market-opening through the cumulation provisions to allow sales into Mexico and Canada – will allow the U.S. industry to out-compete China. In the absence of improved options for maintaining apparel manufacturing in this hemisphere, the practical effect of renewed quota restrictions on China will be to shift production to other Asian suppliers, such as India and Pakistan.

Of course there are instances when the use of the China textile safeguard is appropriate. Those instances meet three criteria: 1) the product is no longer subject to quota when the safeguard is requested, 2) the United States actually produces the product at issue, and 3) there is a legitimate demonstration of market disruption. An increase in imports by itself does not equal market disruption. In addition to a rapid and significant increase in imports, market disruption historically has been demonstrated through a thorough review of a range of factors having a bearing on the evolution of the state of the industry, including turnover, market share, profits, export performance, employment, volume of disruptive and other imports, production, utilization of capacity, productivity and investments.

The textile safeguard included as Paragraphs 241 and 242 of the Working Party Report on China's accession to the WTO had its origins in the "consultation mechanism" that was included in every bilateral textile agreement the United States had with China since 1980. The terms of Paragraph 242 actually represent a multilateralized version of two provisions contained in the bilateral textile agreement reached between China and the United States in 1997 (paragraphs 8 and 21).

It is apparent that the textile safeguard mechanism was not intended to be used before goods became quota-free. Even the predecessor organization to NCTO – ATMI – recognized this. We note that in September 2002 ATMI issued a press release which expressly acknowledged that "The use of the temporary quota is allowed until December 31, 2008 only for products that have already been removed from quota-control under the terms of the WTO Agreement on Textiles and Clothing." The Bush Administration also recognized this, as evidenced by the press release issued by the Commerce Department in April 2003, which expressly described the China textile safeguard mechanism as applicable to "imports of textile and apparel products from China that have been `integrated' (i.e. removed from quota) into the WTO trade regime."

That press release announced the establishment of U.S. procedures for considering whether to take safeguard actions, either in response to requests from private parties or through self-initiation by the Administration. Those procedures, published in the Federal Register in May 2003, were intended to implement the textile safeguard.

Regrettably, the domestic textile industry decided in 2004 that it was not content with abiding by the rules both the United States and China agreed upon as part of the 1997 bilateral textile agreement and again as part of the China accession agreement. Starting in the summer of 2004, the industry began pressing the Administration to disregard those rules and allow the industry to get a jump-start on new restrictions. It is apparent that both the industry and the Administration understood full well that initiating a safeguard measure before products were even quota-free is not permissible under the Accession Agreement. Proof of the Administration's view is clear from its own press release, from the wording of the May 2003 procedures, as well as from a letter from the chairman of the Committee for the Implementation of Textile Agreements expressly rejecting a July 2003 safeguard request because it covered products that were not yet integrated. Even Members of Congress recognized that the textile safeguard was not applicable to products still under quota, so they introduced legislation, H.R. 5026, to instruct the Administration to disregard the agreed rules.

That brings us to the third question raised by the Commission. The willingness of the Administration to consider and act upon requests for safeguard measures even before products were quota-free, and whether that is a violation of U.S. law, is now the focus of a lawsuit brought by USA-ITA on December 1. That case is pending before the U.S. Court of International Trade and it would be inappropriate for USA-ITA to argue its case before this Commission. However, we can say that the suit is about much more than trade with China. The suit is about whether the public has a right to prior notice when the Government wants to change its rules or its interpretation of its rules, and whether the public should be permitted to comment on new rules before they are actually implemented.

Obviously, that sounds a lot less intriguing than an international dispute pitting top name importers and retailers against U.S. mills trying to cope with a new onslaught of competition when a decades-old quota system is finally dismantled. But viewed in its actual terms, the case is a lot more important to basic American values, the democratic process and promotion of the concept of transparency, than about China.

At the center of *USA-ITA v. United States* is the May 2003 Federal Register notice. Before May 2003, CITA decided in complete secrecy whether to impose new textile quotas. The

first public notice of a new quota would come when CITA issued a Federal Register notice revealing that it had already requested consultations with a foreign government to establish a new quota. But the May 2003 notice told private parties – domestic producers and importers alike – that a three step process would henceforth determine whether new quotas would be established for Chinese goods. First, if a private party request were submitted, CITA would take 15 days to decide whether it met the minimum requirements for a request. Second, if the request was sufficient, or if CITA wanted to self-initiate consideration of a safeguard measure, a 30-day public comment period would follow. Third, following the comment period, CITA would take up to 60 days, and perhaps more if necessary, to decide whether a safeguard was appropriate. If the decision was to approve the request or self-initiation, CITA would request consultations with China. Requesting consultations also would determine the quota period and the quota level. The quota would apply to goods exported from China on or after the date the consultations were requested. The quota level would be based upon U.S. imports from China during the one year period ending two months before the month in which the request was presented, plus 7.5 percent for cotton and man-made fiber products or 6 percent for wool products.

USA-ITA charges that CITA violated its own rules by considering safeguards before products were integrated and violated the Administrative Procedures Act by failing to provide private parties with fair notice of a change in these important rules. The issue of whether CITA has authority to implement the safeguard provision of China's Accession Agreement is also before the Court. violates U.S. law. Is CITA above or outside the law when all other federal agencies have to follow such rules, and when producers and importers of products other than textiles have the right to notice and to comment? That is what the U.S. Court of International Trade will decide.

Finally, the last question from the Commission is about the impact of the recently-announced China export tax on textile and apparel products. Our understanding is that the purpose of the Chinese decision was to try to eliminate some of the fears of developing country manufacturers, as well as U.S. companies, that once the quotas were removed, the prices for Chinese shipments would decrease and put pressure on global prices. It is too soon to say what the impact of this measure will be or whether it is the only measure China will take in response to the concerns.

Thank you for this opportunity to provide the views of the importing sector of the textile and apparel industry in the United States. China's accession to the WTO presents important opportunities and challenges for all of us, and we look forward to meeting them.