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The underlying EU law and what it takes to change the law

China is clearly defined as a Non Market Economy (NME) in EU law.

Article 2(7) of the basic Anti-Dumping Regulation (Regulation 1225/2009) allows the use of the analogue country methodology for determining Normal Value for NMEs.

If the EU is to change the methodology for determining Normal Value in relation to goods from China there has to be a change in the law. This is why the EU is the first mover on interpreting Section 15 of China's WTO Protocol of Accession.

Changing the provisions of the basic EU anti-dumping Regulation requires a legislative proposal from the EU Commission and the assent of the EU Council (made up of the 28 Member States) and the European Parliament (directly elected by EU citizens). Slightly differently from the US, where there is a difference of opinion between the two chambers of the legislature, the resolution is reached in a *trilogue* between the Commission, the Council and the Parliament.

The EU Commission has indicated that it will make a legislative proposal in relation to China before the summer of 2016. It hopes that the two chambers will be able to reach agreement on the proposal such that change (if that is what is proposed) can be effected before December 2016 or, if not, that the EU will have sufficiently progressed towards change that China would not initiate dispute settlement in the WTO.

This is an ambitious timetable. Normally, in the best case scenario, it takes one year for a legislative proposal to be adopted in the EU. Changing the law in relation to China would not be in the best case scenario.

Among the Member States, only Italy has expressed an opinion against recognizing China as an NME. However, that many other Member States have informally expressed views against granting market status to China. Overall it is difficult to call the issue.

In the European Parliament the second largest grouping has come out against MES and the largest group is moving in that direction.

In this scenario the approach taken by the Commission in its legislative proposal is crucial to the possibility of reaching agreement.

Does the Commission consider China a Market Economy?

The Commission does not consider that China is a market economy.

In 2003 a dialogue was initiated between China and the EU on the nature of China's economy. China sought to show that its economy met the five criteria set out in EU practice to determine



the nature of an economy. The five EU criteria are not materially different from those of the US. The five criteria are:

- decisions of firms regarding prices, costs and inputs, including for instance raw materials, cost of technology and labour, output, sales and investment, are made in response to market signals reflecting supply and demand, and without significant State interference in this regard, and costs of major inputs substantially reflect market values;
- firms have one clear set of basic accounting records which are independently audited in line with international accounting standards and are applied for all purposes;
- the production costs and financial situation of firms are not subject to significant distortions carried over from the former non-market economy system, in particular in relation to depreciation of assets, other write-offs, barter trade and payment via compensation of debts;
- the firms concerned are subject to bankruptcy and property laws which guarantee legal certainty and stability for the operation of firms;
- and exchange rate conversions are carried out at the market rate.

In a 2008 report the Commission concluded:

The conclusion of this report is that China now has in place almost all the legislation which is necessary for granting of Market Economy Status. That is a considerable achievement. The focus has now switched to the effective implementation of these laws which are crucial for the functioning of any market economy. Market Economy status is assessed on the basis of five criteria. In the judgement of the European Commission, China has clearly fulfilled one of these criteria, Criterion 2 which relates to the absence of state intervention in enterprises linked to privatisation and the absence of non-market forms of exchange or compensation such as barter trade. China has made considerable progress on the remaining four.

In a 2011 report the Commission did not materially change its views.

In 2013, we understand that China informed the Commission that it did not wish to continue the dialogue. So no further evaluation has been made. It can be concluded that the Commission views from 2008 and 2011 remain the Commission view today.

Thus the formal position of the Commission is that China is not a market economy. In recent months this finding that China is not a market economy has been reaffirmed in numerous statements both from Commissioners and Commission staffers. It can also be seen in the text of the Inception Impact Assessment document (see below).

If China is not a Market Economy why change the law?

A legal opinion from the Legal Service the Commission states that the EU is obliged, on the basis of the Legal Service's interpretation of Section 15 of China's WTO Protocol of Accession, to treat China as a market economy for the purposes of determining Normal Value. This legal opinion seems to be driving Commission thinking on the issue.



The Commission has not taken on board the fact that there are legal opinions which reach different conclusions. Given its importance and the fact that it is openly contested, it is surprising that the opinion has not been made public. The concern is that it is results orientated rather than analytical.

Most importantly, the Legal Service of the European Parliament, in a more detailed and comprehensive analysis, has reached a conclusion different from the Commission and considers that the provisions of Section 15 do not provide that the EU must consider China a Market Economy or clearly indicate what methodologies must be used for determining Normal Value after December 2016.

Neither of the opinions are publicly available. However, the Parliament's opinion has been leaked to the press. And Commissioner Malmström has said publicly that the Commission legal position is that MES must be granted.

What is current Commission thinking?

For the EU Commission it appears that a distinction can be made between the nature of the Chinese economy, is it or is it not a market economy, and the methodology that must be used to determine Normal Value after December 2016.

This distinction is reflected in two documents recently made public: i) an Inception Impact Assessment and ii) an Open public consultation regarding a change in methodology in TDI cases.

The Impact Assessment looks to evaluate the consequences of the different options available to the EU: i) maintain status quo; ii) remove China from the list of NMEs in the basic AD Regulation but allowing, where a sector is NME, use of non-China costs and prices; iii) remove the analogue country approach but re-enforce the normal TDI instruments in various ways. The Impact Assessment is expected for May 2016.

The Public Consultation asks a series of questions to stakeholders on the implications of the expiry of part of Section 15 of the Protocol of Accession as well as the functionality of the changes to the TDI instruments.

Next Steps

The College of Commission will meet during the summer of 2016 to decide what approach to take.

If the Commission proposes legislative change the Parliament and the Council will begin review of the proposal in the Autumn of 2016.

Agreement between the two Chambers will be difficult to achieve.

China is not a market economy

China is not a market economy. China itself calls its market a Socialist Market Economy. It is clear that China is different from the socialist economies in the Soviet Union and Eastern Europe in the 40 years after the second World War. China uses different tools for managing



the economy. There are currently 72 Five Year Plans applicable in China at a national, provincial and industry sector level.

These plans have resulted in the massive build up of overcapacities in certain sectors. Bankruptcy and anti-trust laws are not enforced. The ‘market’ is not allowed to function to reward winners and eliminate losers.

Section 15 of China’s WTO Accession Protocol

Here I strongly share the views of my colleague Mr. Price. Section 15 paragraph (d) clearly provides that it is China which must show that it is a market economy. It is not up to the EU or the US to grant it unilaterally. The criteria to be met are those of the importing WTO Member.

The expiry of paragraph (a)(ii) in December 2016 does not mandate the use of any particular methodology for determining Normal Value after that date.

In fact the use of Chinese costs and prices is only mandated if the producers under investigation can show that market economy conditions prevail in their sector.

If China is not a market economy then the use of Chinese costs and prices for determining Normal Value is inherently inappropriate as they are, in fact and in law, distorted by the nature of the economy that gives rise to them.

Section 15 must be read in conjunction with Section 9 of China’s WTO Accession Protocol. In Section 9 China committed to allowing all prices to be set by the market with some exceptions for pharmaceuticals and certain vital services. China has not met that commitment. If prices were set by the market there would be no need for the provisions of Section 15.

The US and the EU

The US and the EU are currently negotiating the TransAtlantic Trade and Partnership Agreement. US industry hopes to benefit from better access to the EU market.

If, at the same time, the EU was to start calculating Normal Value on the basis of Chinese costs and prices it would, in effect, undermine the effectiveness of the EU anti-dumping instrument allowing massive dumping onto the EU market.

In this scenario the benefit that the US might get from TTIP would be undermined by unfair Chinese trade into the EU.

Conclusions

It is in the interest of the US to ensure that the EU does not grant MES to China. Thus the US should make its legal interpretation of the meaning of Section 15 of the Accession Protocol known to the EU.

The text of Section 15 was negotiated between the US and China. Towards the end of those negotiations the parties agreed that the expiry provisions should only apply to paragraph (a)(ii) and not to all of paragraph (a). This change was to allow the continued use of methodologies other than Chinese costs and prices for determining Normal Value.



The final determination of how Section 15 should be interpreted will be made in WTO dispute settlement. If the US view is to succeed in that forum it is essential that its main trading partner supports its views. The US must now ensure that the EU does not prejudice its position by taking a different view.

Any legislative proposal by the Commission to grant MES or its equivalent to China would already prejudice WTO dispute settlement even if that proposal was not adopted by the EU legislator.