

CRS Report for Congress

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China and the World Trade Organization

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Summary

After many years of difficult negotiations, China, on December 11, 2001, became a member of the World Trade Organization (WTO), the international agency that administers multilateral trade rules. Under the terms of its WTO membership, China agreed to significantly liberalize its trade and investment regimes. A main concern for Congress is to ensure that China fully complies with its WTO commitments. According to U.S. government officials and many business representatives, China's WTO compliance record has been mixed.. This report will be updated as events warrant.

After 15 years of bilateral and multilateral negotiations, China formally entered the WTO on December 11, 2001. The negotiations on China's accession to the WTO focused on many Chinese practices that distort flows of trade to and from China, such as high tariffs and non-tariff barriers, restrictions on foreign investment, lack of national treatment for foreign firms, inadequate protection of intellectual property rights (IPR), and trade-distorting government subsidies. Membership in the WTO requires China to change many laws, institutions, and policies to bring them into conformity with WTO rules.¹

The Role and Interest of the United States

China has been one of the world's fastest growing economies over the past several years (real GDP growth averaged 9.3% annually from 1979 to 2003), and many trade analysts argue that China could become a potentially large market for a wide variety of U.S. goods and services. A World Bank report estimates that China's share of world trade could triple from 3.0% in 1992 to 9.8% by the year 2020, making China the world's second-largest trading nation after the United States.² The growing importance of China in the world economy was an important factor in the heightened interest among WTO members in bringing China into the WTO and thereby subjecting its trade regime to multilateral trade rules.

¹ See also CRS Issue Brief IB91121, *China-U.S. Trade Issues*, by (name redacted).

² The World Bank, *China 2020: China Engaged*, 1997, p. 31.

U.S. trade officials insisted that China's entry into the WTO had to be based on "commercially meaningful terms" that would require China to significantly reduce trade and investment barriers within a relatively short period of time. Many U.S. trade analysts viewed China's WTO accession process as an opportunity for gaining substantially greater access to China's market and to help reduce the large and increasing U.S.-China trade imbalance. Other U.S. proponents of China's WTO membership contended that it would advance the cause of human rights in China by enhancing the rule of law there for business activities, diminishing the central government's control over the economy and promoting the expansion of the private sector in China.

China Joins the WTO

China completed all of its WTO bilateral agreements on September 13, 2001 (it concluded an agreement with the United States on November 15, 1999) and completed negotiations with the WTO Working Party handling its accession bid on September 17, 2001. China's WTO membership was formally approved by the WTO on November 10, 2001, and on the following day, China informed the WTO that it had ratified the WTO agreements. As a result, China officially joined the WTO on December 11, 2001. Under the WTO accession agreement, China agreed to:

- Bind all tariffs. The average tariff for industrial goods will fall to 8.9% and to 15% for agriculture, with most tariff cuts to occur by 2004 and all cuts by 2010.
- Limit subsidies for agricultural production to 8.5% of the value of farm output and will not maintain export subsidies on agricultural exports.
- Within three years of accession, grant full trade and distribution rights to foreign enterprises (with some exceptions, such as for certain agricultural products, minerals, and fuels).
- Provide non-discriminatory treatment to all WTO members. Foreign firms in China will be treated no less favorably than Chinese firms for trade purposes. Dual pricing practices will be eliminated as well as differences in the treatment of goods produced in China for the domestic market as oppose to those goods produced for export. Price controls will not be used to provide protection to Chinese firms.
- Implement the Trade-Related Aspects of Intellectual Property Rights (TRIPs) Agreement upon accession.
- Accept a 12-year safeguard mechanism, available to other WTO members in cases where a surge in Chinese exports cause or threaten to cause market disruption to domestic producers.
- Fully open the banking system to foreign financial institutions within five years. Joint ventures in insurance and telecommunication will be permitted (with various degrees of foreign ownership allowed).

WTO Implementation Issues

China's implementation of its WTO commitments has been closely followed by U.S. officials and various business groups. On December 11, 2002, the USTR released its first annual China WTO compliance report.³ Although stating that China had made significant overall progress in meeting its WTO obligations, the report raised serious concerns over China's compliance with its commitments on agriculture, services, IPR protection, and transparency of trade laws and regulations. The USTR's second annual China compliance report (issued in December 2003)⁴ again emphasized that China had made significant overall progress in meeting its WTO obligations, but raised concerns over China's compliance with its commitments on agriculture, services, IPR protection, tax policies, transparency of trade laws and regulations, and trading rights and distribution services.⁵ U.S. business groups have raised similar concerns. The U.S.-China Business Council (USCBC) mid-year 2003 report on China's WTO implementation stated that there were "growing concerns" among U.S. firms over China's ability to deliver on key commitments on time and in full.⁶ Finally, a survey of U.S. firms doing business in China conducted by the General Accounting Office in 2003 found that a majority of those questioned felt that China had implemented most of its WTO obligations only to some or little extent.⁷

U.S. officials have raised a number of WTO implementation issues with Chinese officials over the past year:

- **Soybeans.** U.S. soybean exporters have faced uncertainty and, in some instances, disruption in their soybean sales to China, stemming from China's announcement in 2001 that it would soon implement new rules on bio-engineered foods (effective in 2002). China initially failed to provide details of these rules, which led to a disruption in U.S. soybean exports to China from January-March 2002. President Bush personally raised the issue with Chinese officials, which led China to agree to the interim use of U.S. and foreign safety certificates until China implements its new biotechnology regulations. On October 18, 2002, China issued regulations applying this policy through September 2003; the USTR's office stated that the regulation "should remove the threat of an interruption of U.S. soybean sales to China."⁸ In July 2003 China further extended the policy through April 2004. However, U.S. exporters have complained that the regulations require each GMO shipment have an

³ USTR, *2002 Report to Congress on China's WTO Compliance*, December 11, 2002.

⁴ USTR, *2003 Report to Congress on China's WTO Compliance*, December 11, 2003

⁵ The USTR noted that China had made progress in implementing its commitments on the administration of tariff rate quotas on agricultural products, removing restrictions on soybean imports, reduced capital requirements for certain financial service providers and restrictions on auto financing, and ended discriminatory tax policies on information technology products.

⁶ USCBC, *China's WTO Implementation: A Mid-Year Assessment*, June 2003.

⁷ General Accounting Office, *World Trade Organization: U.S. Companies' Views on China's Implementation of Its Commitments*, March 2004.

⁸ USTR Press Release, October 18, 2003.

interim biotech safety certificate and a Chinese government import license. Additionally, in January 2003, the Chinese government indicated that it might delay permanent approval of various GMO crops and might require another round of food safety studies, a move that led the U.S. to issue an official protest. Some analysts charge that China may be attempting to use such regulations to limit biotech imports in order to protect its domestic producers as well as its own biotech industries. U.S. officials have warned that they make take this issue to the WTO for resolution. Despite these problems, U.S. soybean exports to China more than tripled in 2003 (over 2002 levels), making China the largest market for U.S. soybean exports in 2003.⁹

- **Tariff-rate quotas.** In November 2001, the Chinese government developed new rules on tariff-rate-quotas on certain agricultural products that the U.S. charged were discriminatory and violated WTO rules because they created two categories of import quota licenses: one for domestic consumption and one for “processing” trade. The U.S. further charged that China has failed to provide adequate information on the administration of its tariff-rate quotas (TRQs) for farm commodities. In July 2002, the U.S. Department of Agriculture (USDA) reported that China’s TRQ licenses had authorized relatively small levels of imports, making their use impractical.¹⁰ U.S. firms charge that this allocation policy violates WTO rules on national treatment. In other instances, China announced TRQs for various agriculture and manufactured products several months after their required implementation date. In December 2002, USTR Robert Zoellick sent a letter to the Chinese government expressing U.S. concern over China’s administration of TRQs. In January 2003, Zoellick was quoted in the press as saying that the TRQ issue was “one of the areas we’re most frustrated with” in terms of China’s WTO compliance, and warned the United States was considering bringing a dispute resolution case to the WTO. In October 2003, China reportedly issued new regulations (effective January 2004) eliminating sub-quotas and restrictive license procedures, and improving transparency in identifying quota allocation recipients. However, problems appear to remain. For example, China has failed to publish the details of its 2004 TRQ allocation,¹¹ and in March 2004, the National Cotton Council charged that China continues to maintain two categories of import quota licenses for cotton.¹²

⁹ However, U.S. soybean exports to China during the first five months of 2004 declined by 32% over the same period in 2003.

¹⁰ For example, under the WTO accession agreement, China’s TRQ for cotton in 2002 was 818,500 tons. In June 2002, China announced that 500,000 tons of the TRQ would be allocated for processing trade, 270,000 tons for state-owned mills, and 48,500 tons for private mills.

¹¹ *Inside U.S.-China Trade*, February 11, 2004.

¹² Despite these problems, U.S. cotton exports to China have increased sharply in recent years, growing from \$144 million in 2002 to \$761 million in 2003. During the first five months of
(continued...)

- **Export subsidies and discriminatory taxes.** U.S. officials charge that China has subsidized grain exports (mainly corn) and cotton, and uses its tax system to discourage imports and encourage foreign firms to produce domestically, contrary to its WTO commitments. For example, China continues to give rebates on value-added taxes (VAT) for certain industries, especially for high tech. In some instances, China imposes higher VAT rates on certain imported products (such as fertilizers and various agricultural products) than it does for similar products produced domestically. On March 18, 2004, the USTR announced that it had filed a WTO dispute resolution case against China over its discriminatory tax treatment of imported semiconductors, charging that China applies a 17% VAT rate on semiconductor chips that are imported into China but gives a substantial rebate of the tax if the semiconductors are produced or designed in China. On July 8, 2004, China agreed to this policy.
- **IPR.** While China has enacted a variety of new IPR laws and periodical crackdowns on IPR violators, the piracy rate in China for copyrighted products is estimated to be at 90%. The Chinese government estimates the value of pirated goods made in China at \$19 to \$24 billion. U.S. industry officials estimate that IPR piracy in China cost U.S. firms \$2.6 billion in lost sales in 2003. Some members of Congress have called on the Administration to bring a case against China in the WTO over its lack of IPR enforcement. In April 2004, China pledged to “significantly reduce” IPR infringement levels by increasing efforts to halt production, imports, and sales of counterfeit goods, and lowering the threshold for criminal prosecution of IPR violations.

Some analysts argue that China’s compliance with its WTO obligations is being hampered by resistance to reforms by central and local government officials seeking to protect or promote industries under their jurisdictions, government corruption, and lack of resources devoted by the central government to ensure that WTO reforms are carried out in a uniform and consistent manner (especially in regards to IPR enforcement). Although Chinese government officials have promised to implement WTO related reforms, it appears that they are concerned that trade liberalization could cause major employment disruptions in certain sensitive sectors, especially agriculture, that could result in social instability. In addition, many observers charge that, because the Chinese government is trying to promote the development of various industries (especially high tech) it deems critical for the country’s future economic development, it continues to maintain policies that discriminate against imports in favor of domestic industries and/or foreign-invested firms in China.

Despite the persistence of trade disputes between the United States and China, U.S. exports to China have risen sharply since China became a member of the WTO. Between 2001 and 2003, U.S. exports to China have rose by 48%, making China the fastest

¹² (...continued)

2004, U.S. cotton exports to China totaled \$1.1 billion.

growing U.S. export market.¹³ **Table 1** lists U.S. exports of selected products that were a U.S. priority for liberalization during negotiations for China's WTO accession. Some priority U.S. exports have risen sharply (in both dollar and percentage terms), such as poultry, soybeans, cotton, semiconductors, and autos and auto parts, while exports of other priority products, such as corn, alcohol, and fertilizers, have risen more moderately.

Table 1. Selected U.S. Exports to China: 2001-2003
(\$ in millions)

	2001	2002	2003	2001-2003 % Change
Total U.S. exports to China	19,234.8	22,052.7	28,418.9	47.7
Corn	0.6	2.2	0.7	16.7
Wheat	21.4	25.9	35.2	64.5
Poultry meat	39.0	51.2	102.3	162.3
Soybeans	1,012.5	888.7	2,830.3	179.5
Vegetable oils	9.3	16.3	31.7	240.9
Cotton	42.9	143.5	760.8	1,673.4
Semiconductors and related devices	1,074.7	1,585.4	2,448.3	127.8
Fertilizers	421.4	675.4	469.8	11.5
Pharmaceuticals	112.7	191.0	201.7	79.0
Spirits and alcoholic beverages	4.1	5.7	5.6	36.6
Motor vehicles and parts	272.9	385.9	614.5	125.2

Source: USITC Trade Dataweb.

Congress will likely continue to press the Bush Administration to ensure China's compliance with its WTO commitments. Many U.S. business and labor representatives have complained over a number of Chinese trade practices which they claim harm U.S. economic interests, including dumping, subsidization of state firms, "currency manipulation," and unfair labor practices. Some Members have called on the Administration to more aggressively use the WTO dispute resolution mechanism and/or various U.S. trade laws (such as Section 301) to address China's non-compliance with its WTO and other "unfair trade practices."

¹³ During the first five months of 2004, U.S. exports to China were rose by 38% over exports during the same period in 2003.

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